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ABSTRACT

The 12th publication in a series of subject presentations in the field of administrative management for use by educators and businessmen who teach management courses is presented. These presentations are intended to be particularly useful to Distributive Education in the smaller community where library research facilities are limited and equipment for the production of visual aids is not readily available. The lecture is designed to be presented to the businessman in nontechnical language. The Lesson Plan is an outline of the material covered which may be used as a teaching guide. The Presentation may be used as written or modified to meet local needs and conditions. The Visual Aids are photographic copies of the set of visual aids which are available for this topic. These visuals are 8- by 10-inch colored transparencies prepared for use on overhead projectors. The Supply Department contains materials which may be reproduced locally for distribution to course participants. Cases in Point are short actual small-business management cases which may be used to augment the presentation and to develop discussion. The Incubator contains ideas for stimulating further thought and discussion by the participants. A bibliography and list of Small Business Administration field offices are included. (CK)

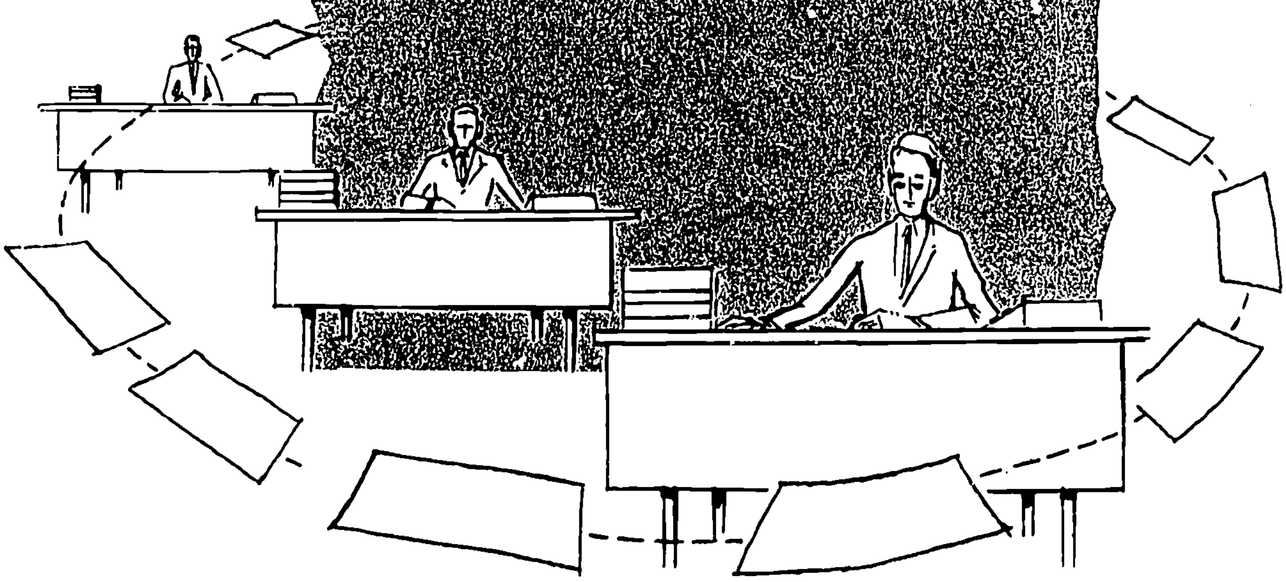
F-X

SAFEGUARDING YOUR BUSINESS AND MANAGEMENT SUCCESSION

ADMINISTRATIVE MANAGEMENT COURSE PROGRAM
Topic 12

SMALL BUSINESS ADMINISTRATION

SAFEGUARDING YOUR BUSINESS AND MANAGEMENT SUCCESSION



ADMINISTRATIVE MANAGEMENT COURSE PROGRAM

Topic 12

Small Business Administration

Washington, D.C. 20416 1965

SMALL BUSINESS ADMINISTRATION

PROCUREMENT AND MANAGEMENT ASSISTANCE

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FOREWORD

The Administrative Management Course Program was developed by the Small Business Administration in cooperation with educational institutions to bring modern management knowledge and techniques to the owners and managers of small businesses. Within 10 years nearly 900 universities, colleges, and local school systems have cosponsored almost 4,000 courses with this Agency. Over 110,000 owners and managers of small businesses have attended these courses. Distributive Education, working through the local school systems, has accounted for about one-third of these totals.

This is an outstanding demonstration of public spirit and service on the part of these hundreds of educational institutions. Yet, there remain many thousands of small-business owners and managers who have never had the opportunity to attend an administrative management course.

A committee on management education, consisting of representatives of the Small Business Administration and the Distributive Education Division of the American Vocational Association, was formed to study ways of meeting the small-business management needs of the small communities and very small businesses in poverty areas. The committee recommended that a series of subject presentations, including lesson plans, lectures, visual aids, case studies, and handout material, be developed to assist in the establishment of administrative management course programs in new locations. Further, it was felt that this material could substantially assist existing management programs, particularly by emphasizing the importance of continuing education for small-business owners and managers, and by assisting the busy instructor with his preparation.

SBA accepted the responsibility for developing a series of subject presentations in the field of administrative management for use by educators and businessmen who teach these management courses. We believe that these presentations will be particularly useful to Distributive Education in the smaller community where library research facilities are limited and equipment for the production of visual aids is not readily available. They will also assist community planning groups in implementing the educational provisions of the Economic Opportunity Act of 1964.

The booklet was developed by the Courses and Conferences Division. I wish to express appreciation to the Richmond Public Schools System for granting leave of absence to John O. Perreault, who drafted the booklet. The final version was prepared under the administrative direction of George C. Willman, Jr., Acting Chief of the Division. Artwork for the cover was prepared by Michael J. Fontana of the Graphics and Design Branch, Office of Administrative Services.

Irving Maness
Deputy Administrator

September 1965

CONTENTS

*A set of the visual aids is available from the nearest SBA office (see inside back cover). These visuals are 8- by 10-inch colored transparencies for use on overhead projectors.

**Among the materials prepared as "handouts" to participants are several SBA free publications. Current information on the availability of suggested and new SBA publications may be obtained from the nearest SBA office.

A WORD ABOUT THIS SESSION

This publication, one of a series, is directed toward teaching management skills to the small-business man. When the term "management" is used, it refers to administrative management functions rather than to purely operational features of business. The complete set of subject presentations may be obtained on loan from the nearest Small Business Administration field office (listed on the inside back cover). Single booklets or complete sets may be purchased from the Superintendent of Documents, Washington, D.C. 20402.

This topic, *Safeguarding Your Business and Management Succession*, was prepared to aid in teaching one session of a basic course. It contains sufficient material for a 45- to 60-minute lecture which is usually followed by a discussion period. The management case on page 61 can be used to extend the session or to form the basis for a second session on the topic.

The lecture is designed to be presented to the businessman in nontechnical language. It is *one* approach to teaching financial management. Instructors will probably prefer to modify or revise the lecture in order to use their personal background and experience in the subject area. They may also find it preferable to alter the topic to take account of the training or special needs of their class participants.

This topic may be handled by a management consultant, a retired businessman, or another whose training, experience, and interest qualify him. *Guide for Part-Time Instructors, Distributive Education for Adults*, a publication of the U.S. Office of Education, may prove useful to local instructors.

The various sections of the publication are separated by divider sheets of different colors. On the following page, these colors are given and the contents of the sections are briefly described.

Gray—*The Lesson Plan.* An outline of the material covered which may be used as a teaching guide, or as a framework for developing an individualized presentation. The lesson plan contains two columns: the left-hand column is an outline of the presentation; the right is a step-by-step indication of procedure, including chalk-board suggestions, quotations, discussion points, and a keyed guide to the visual aids supplied.

Rust—*The Presentation.* A carefully prepared subject presentation which may be used as written or modified to meet local needs and conditions. It may also be used as a source of information by a person preparing his own lecture.

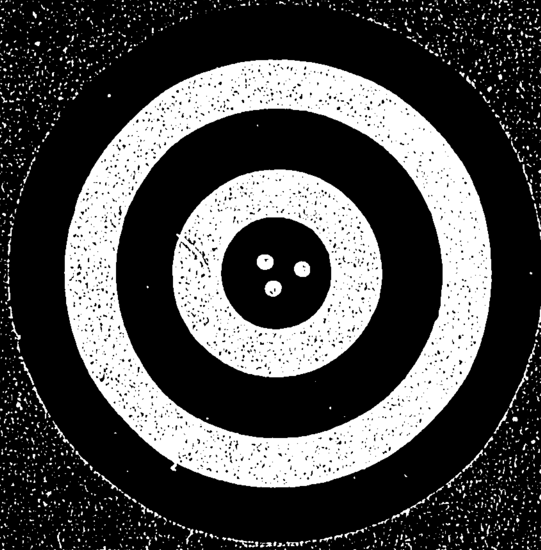
Buff—*The Visual Aids.* Photographic copies of the set of visual aids which are available for this topic. These visuals are 8- by 10-inch colored transparencies prepared for use on overhead projectors. The subject presentation and lesson plan are keyed to the visuals. A set of visuals for each subject in this series may be borrowed from the nearest SBA regional office.

Green—*The Supply Department.* Materials which may be reproduced locally for distribution to course participants. Your nearest SBA office can furnish information on current availability of SBA free publications, including titles published subsequent to this volume.

Yellow—*Cases in Point.* Short actual small-business management cases which may be used to augment the presentation and to develop discussion, or as the basis for a second session on the same topic.

Blue—*The Incubator.* Ideas for stimulating further thought and discussion by the participants. This material may be reproduced locally for distribution to course participants. "Assignments" are designed to aid in retention of the subject matter of the session.

NOTE: See back cover for index reference to the divider sheets.



THE LESSON PLAN

A Keeping on Target

Section

Good teaching depends on good planning. [illegible] will enable you to keep instruction [illegible] on the target.

The primary aim of the instructor [illegible] he MUST KNOW [illegible] SHOULD KNOW. [illegible]

The following lesson plan [illegible]

STIMULATE GROUP BY SERVING AN INSTRUCTIONAL COCKTAIL

RECIPE

Use The Three B's (Bubbles)

- O ***Base*** instruction on problems at learners level.
- O ***Blend*** instruction with job experience.
- O ***Brighten*** instructions with variety of ***illustrations, investigations*** and group ***participation.***

FOUR BASIC STEPS OF INSTRUCTION

Instructing is like selling - -

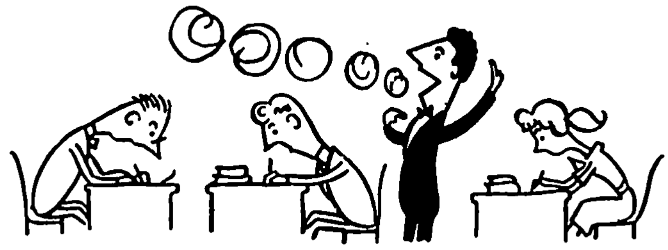
Selling

1. Approach customer
   - Promptness
   - Put at ease
   - Awaken ***interest***
2. Present merchandise or service
   - Select merchandise to fit need
   - Show one item at a time
   - Demonstrate ***selling points***
3. Have customer take part
   - Get merchandise into customer's hands
   - Let customer "try on" merchandise
   - Answer questions and meet objections
4. Bring sale to close
   - Help customers decide; ask: "which" "for whom" "when"
   - Be sure merchandise fits need
   - Summarize points of care and use
   - Handle mechanics of sale
   - Pave way for return visit

Instructing

1. Prepare the group
   - Start on schedule
   - Put group at ease
   - ***Awaken*** interest
2. Present information
   - Gauge material to needs
   - Present one point at a time
   - ***Show, illustrate, question***
3. Have group participate
   - Get group to ***discuss***
   - Have members ***demonstrate*** or ***use*** ideas
   - Answer questions and correct errors
4. Bring meeting to a close
   - Check on understanding; ask: "why" "how" "when" "what" "where" "who"
   - Be sure group now can use information
   - Summarize "take away" ideas
   - Make a definite conclusion
   - Pave way for next session

How To Deal With "Difficult Customers"



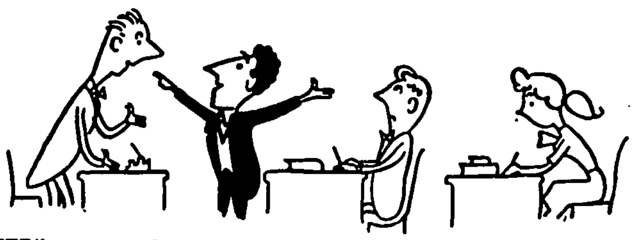
What To Do

THE "MOUTH"—wants to do all the talking.

Take the play away from him by asking others to comment on his remarks.

Deliberately turn to others and ask for their opinions. Avoid looking at him.

Tactfully ask him to give someone else a chance, or talk to him in private.



THE "ARGUER"—constantly tries to catch you up.

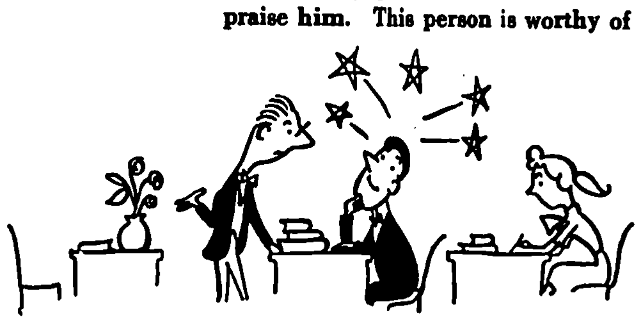
Keep cool. You can never "win" an argument. Always make him back it up. Ask for evidence.

Avoid getting personal.

Refer the question to the group and then to him.

THE "MOUSE"—is in every group.

Call him by name and ask him for an opinion. Ask him an easy question he is sure to answer well, then praise him. This person is worthy of your attention.



THE "SO-WHATER"—is disinterested.

Point up something he has done as a good example of the point being stressed. Ask direct questions affecting his work.

LESSON PLAN

TOPIC: SAFEGUARDING YOUR BUSINESS AND MANAGEMENT SUCCESSION

OBJECTIVES:

To show the need for a carefully coordinated insurance program.
To outline the various types of insurance a small-business owner may need.
To indicate the importance of a plan for management succession.

SESSION CONTENT	TIPS AND APPROACHES
I. INTRODUCTION A. The future holds many risks B. Insurance can lessen business risks	"Look Mom! It's tomorrow" story or other appropriate introduction.
II. WHAT INSURANCE IS A. Trading a large uncertain loss for a small but known cost B. Insurance is like a guarantee	Visual No. 1 Define insurance
III. WHEN INSURANCE DOESN'T PAY A. Trivial loss B. Unnecessary coverage	Visual No. 2

IV. ALTERNATIVES TO COMMERCIAL INSURANCE

A. Noninsurance

B. Loss prevention

C. Risk transfer

D. Self-insurance

V. POINTERS ON BUYING INSURANCE

A. Selecting an insurer — Visual No. 3

1. Financial stability
2. Field of specialization
3. Flexibility
4. Cost of coverage

B. Selecting an agent — Visual No. 4

1. Contacts among insurers
2. Knowledge
3. Degree of individual attention
4. "Extras"
5. Help in time of loss

VI. TYPES OF COVERAGE

A. Fire insurance — Handout No. 12–1

1. Peril coverage — Handout No. 12–2
2. Property coverage
3. Losses excluded
4. Coverage terms
5. Extended coverage

B. General liability insurance

1. Coverage
2. Exclusion
3. Limitations

C. Automobile liability insurance and automobile physical damage insurance

D. Workman's compensation and employee liability insurance

E. Fidelity bonds

F. Crime insurance

1. Burglary insurance
2. Robbery insurance
3. Comprehensive crime policies
4. Storekeeper's burglary and robbery policy

G. All-risks physical damage contracts

H. Business interruption insurance

I. Power plant insurance

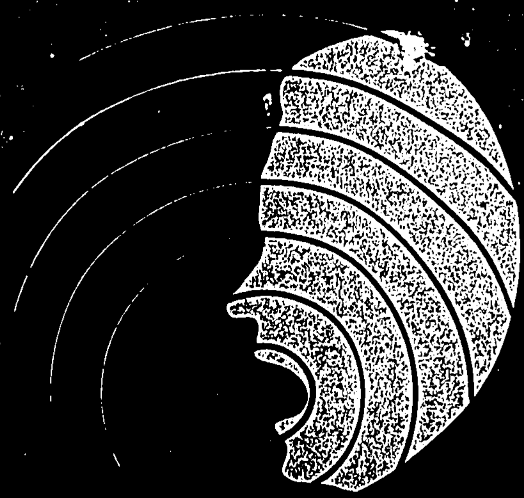
J. Glass insurance

K. Business life insurance

1. Key man insurance
2. Business owners' insurance
3. Business continuation life insurance
4. Cross-purchase and entity plans

VII. MANAGEMENT SUCCESSION	
A. Need for succession plan	Handout No. 12–3
B. Develop a "no. 1 boy"	Visual No. 5
C. Effects of not planning	
D. The succession plan	Visual No. 6
1. The will	Visual No. 7
2. Insurance	Visual No. 8
3. Tax implications	Visual No. 9
4. Management development	Visual No. 10
5. Interim management	Visual No. 11
6. Retirement	Visual No. 12

F. Plans for different types of ownership	
1. Proprietorships 2. Partnerships 3. Corporations	List three types of organization. Discuss individual characteristics.
G. The family business	
1. Ownership succession 2. Management succession	
VIII. SUMMARY AND CONCLUSION (The Last Best Chance)	Hand out Focal Points



SAFEGUARDING YOUR BUSINESS AND MANAGEMENT SUCCESSION

INTRODUCTION

Perhaps you have heard of the incident involving a 9-year-old aboard a transcontinental express. As the roaring train emerged from the long dark tunnel which pierces the continental divide of the Northern Rockies, the astonished child exclaimed, "Look Mom! It's tomorrow."

Any man, experienced with life and the market place, needs no convincing as to the inevitability of tomorrow or of the fact that it can come upon him with all the roaring abruptness of a transcontinental express. Most business and professional men make some provision to protect their families from the risks of the uncertain tomorrows, but, all too frequently, they fail to make the same commonsense provisions for the protection and continuity of the business itself.

One of the ways you can protect yourself against the risks of the future is through insurance, and nowhere is insurance more important than in the management of a business. In many instances, losses in a small firm can mean the difference between growth and failure, vitality and stagnation. Very few small businesses have even a portion of the financial resources available to larger firms. Frequently, they must operate on a very slim margin if they hope to stay in business. Therefore, unexpected losses can hit them hard.

Without adequate insurance, what happens to such a firm when the owner dies or is suddenly incapacitated? When a fire breaks out and destroys the firm's building or stock? When an employee is found to have embezzled company funds? When a customer is awarded a liability judgment for an accident? Too often, the business is forced to the wall, its future operations severely curbed; sometimes, it is damaged beyond repair, its ability to continue completely crushed.

Almost always, a small-business man would find it impossible to handle the full burden of his potential risk. The amount of money he would have to set aside to cover possible losses would leave him nothing, or almost nothing, to run his business

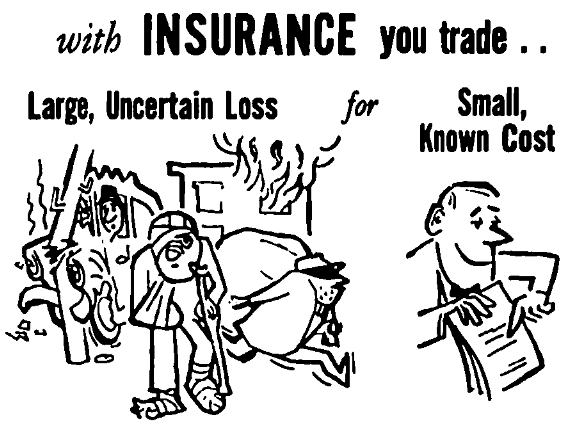
with. If loss were to occur which he could repair by using his reserve fund, what assurance would he have that another loss—the same kind or different—might not occur next week, next month? But then he would have no reserve fund—and little likelihood of staying in business at all.

Insurance is a strong partner in forestalling the damage that the unexpected can do. A well-designed insurance program not only provides for losses, it can also gain other side values difficult to obtain through other means.

WHAT INSURANCE IS

Because insurance is a complex subject, it is little wonder that many are confused about its proper place in the running of businesses. Frequently, businessmen buy "too much" or "too little" coverage or they attempt to insure situations that might better be handled by other means. Often, they do not distinguish between true insurance and the other means of handling risk.

Pure risk exists when a person is faced with a situation in which he has only the possibility of loss. Thus the occurrence of a fire, a windstorm, the death of a key man, the sickness of the owner, or a liability judgment cannot be determined with a degree of certainty and generally causes nothing but loss. Since it is most unusual for these perils to bring about a gain, they may be classified as pure risks.



Visual No. 12—1

The main value of insurance to you is its reduction of the pure risk you face in your operations. Buying insurance gives you the opportunity *to trade a large but uncertain loss for a small but certain cost* (expenditure) called a premium. You trade uncertainty for certainty—which is just another way of saying that you reduce your risk. Insurance has many added values, such as reducing worry, stimulating

initiative, freeing funds for investment, preventing loss, and making credit easier to obtain. But all these values stem from the one central value—risk reduction.

Insurance does not differ greatly from the typical business guarantees for merchandise or services, guarantees of satisfaction, and the like. You actually act as an insurer when you guarantee that your goods will give satisfaction. Because no specific consideration is given by the customer for such a guarantee and because satisfaction is not defined, such business guarantees probably are not legally enforcible insurance contracts, at least in the commonly accepted sense of the term. Yet you should figure in advance the cost of the returned goods privilege and add this cost to gross markup; this is planning for a certain cost, the "premium," which is passed on to customers, who in this sense are those who are insured. A few courts have upheld this concept in the guarantees granted purchasers of used cars.

WHEN INSURANCE DOESN'T PAY

Although there are certain situations in which the commercial insurer may refuse to underwrite a risk, there are others in which you should not use commercial insurance even if offered.

Trivial Loss. If the potential loss is trivial, even if the peril should occur, there is no point in insuring it. It follows that insurance should be purchased first upon losses that are the most severe. What is "trivial" depends upon the financial resources of the businessman.

As long as the *possibility* of loss exists, protection is needed. In one case, a firm reviewed its insurance program and discovered that it was insuring an old house against fire. It was located on a piece of industrial property and was scheduled to be torn down. It would not be replaced even if it were destroyed. When these facts came to the attention of the manager, coverage on the house was canceled.

Unnecessary Coverage. If the cost of purchasing commercial protection is so high that the premium is a substantial proportion of the value of the property, the question arises of whether the insurance should be purchased. It is surprising how often this seemingly simple point is overlooked. For example, it is not uncommon for a firm to purchase $50-deductible collison insurance when it could save $35 annually by purchasing $100-deductible collison insurance. The firm is in effect paying $35 for $50 of extra coverage—70 percent of the possible recovery in the event of a single collision during the policy term. Even if more than one collision occurs, the premium seems prohibitively high.

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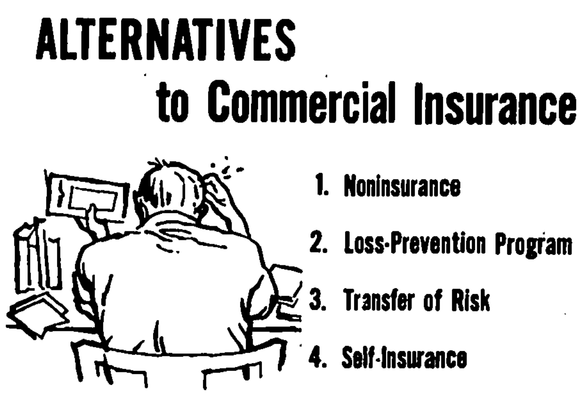
ALTERNATIVES TO COMMERCIAL INSURANCE

Sometimes you can cut your costs of reducing the risks in your business by methods other than commercial insurance. Or you can combine these other methods with commercial insurance to gain savings.

Other than insurance, there are at least four other ways of dealing with risk:

1. Assumption of risk; that is, doing nothing about it (noninsurance).
2. Loss-prevention programs.
3. Transfer of risk to persons other than commercial insurers.
4. Self-insurance.



Visual No. 12—2

Noninsurance. Most business firms find that they must inevitably assume some risks. Buying coverage against every possible risk is impractical for most firms. Yet it is no excuse to say that an insurance premium is "prohibitive" in cost. If you cannot afford the premium, certainly it is unlikely that you can afford the loss if it should occur. It is foolhardy to assume large risks when reasonably priced commercial coverage is available. You should assume the risk only when the severity of the potential loss is low. Also, noninsurance usually should be restricted to risks that are more or less predictable, preventable, or largely reducible. It is ideally suited to risks which are essentially "business risks."

Loss Prevention. Loss-prevention programs actually handle risk indirectly by reducing the probability of loss. Programs to prevent fire, to protect against burglary, to further health maintenance, to provide better and safer building construction usually reduce the costs of operating a business—if not immediately, then over the long run. Also, they will usually result in reductions in the premium charged by a commercial insurer. A loss-prevention program seldom eliminates all losses, but it does reduce their frequency so markedly that commercial insurance protection can often be purchased at a low cost.

Risk Transfer. Transfer of risk to persons other than commercial insurers is often both possible and economical. For example, you can transfer to others the risk of loss resulting from automobile accidents by leasing all your vehicles under an agreement whereby the lessor maintains all insurance. Often, he can obtain a significantly larger spread of loss than you can. Thus he can protect the vehicles at a lower cost.

Self-Insurance. You can successfully be your own insurer if you meet certain requirements. Note that self-insurance differs from noninsurance. In noninsurance, you assume a risk and do nothing about it. In self-insurance, you must actually administer a program of risk management. A program of self-insurance should not be undertaken lightly. Skilled personnel, adequate finance, and widely diversified risks are prerequisites. Often, the small-business man will not be able to meet these requirements because his operations are too limited.

POINTERS ON BUYING INSURANCE

Suppose you have decided that some type of insurance is the best and most economical method of handling a pure risk to which you are exposed. From whom should you purchase commercial insurance coverage? What types of agents and insurers are available? What are the advantages and disadvantages of each type?

As in many parallel situations in tangible goods industries, buying skill is important in the purchase of insurance. In buying raw materials, the price, credit terms, returned goods privileges, and guarantees granted by suppliers are all vital to the success of the businessman. Likewise, vital factors affecting insurance-buying satisfaction include the financial and legal characteristics of the insurer, the services rendered by his agent, and the flexibility of the underwriter in adapting to the particular requirements of an insured. The insurance buyer may need specialized guidance in such matters as choosing the correct types and amounts of insurance, avoiding legal tangles, and setting up the appropriate personnel and other management policies which will help him get the most out of his insurance protection.

Selecting an Insurer

Four major types of insurers operate in the United States today: (1) stock companies; (2) mutual companies; (3) reciprocals; and (4) Lloyds groups. In general, mutual companies and reciprocals are cooperatively organized insurers and offer insurance "at cost," while stock companies and Lloyds groups are profitmaking ventures. In practice, however, the "costs" of the cooperatively owned insurer may be no lower than those of the profitmaking insurer.

In comparing the different types of insurers, you should be interested in the following: (1) the financial stability of the insurer; (2) the type of coverage in which the insurer specializes; (3) the insurer's flexibility in the offering of coverage. Only after these points are satisfied should the insurance buyer compare (4) the costs of protection.

Visual No. 12—3

Financial Stability. Typically, small businessmen rely on the agents through whom they deal to judge the financial stability of their insurance companies. In some cases, however, the agent may not have made a careful analysis or he may be partial toward one of the organizations he represents. If you suspect either situation, you may want to consult sources such as *Best's Insurance Reports* for a financial rating and analysis of a company with which you are going to do business. In purchasing commercial insurance, the purpose is to obtain an outside guaranty that loss claims, if they occur, will be honored and will be paid promptly. An insolvent or financially unstable insurer obviously cannot pay claims or will procrastinate in paying them.

Field of Specialization. Some insurers specialize in certain types of coverage and offer you the advantages of greater experience in those lines. For example, a type of insurer known as a factory mutual specializes in a specific industry—such as lumber. Stock insurance companies have an organization, known as the Factory Insurance Association, which was formed to provide specialization similar to that offered by factory mutuals.

Lloyds groups, particularly the Lloyds of London, often specialize in the types of risks which are sufficiently dangerous to have been refused coverage by other insurers.

Reciprocals often specialize in a given line of insurance, such as automobile insurance, offering low cost as the chief inducement.

Flexibility. It is not realized by many insurance buyers that some insurers will tailor their policies to meet the needs of the buyers. You can have special provisions inserted, make unusual arrangements for determining the final premium, or provide for certain services according to your particular requirements. Depending on the amount of insurance purchased, you can usually bargain with the insurer for special consideration in rating. In the purchase of group life and health insurance, for example, you can arrange for a refund of part of the premium if your losses do not exceed certain predetermined levels.

Cost of Coverage. Once you have satisfied yourself on the points of financial stability, flexibility, and coverage offered by a given insurer, you are in a position to make a cost comparison. Don't make the error of confusing the initial premium with the net premium. Some insurers charge a lower initial rate (called a deviated rate); others charge a higher initial rate but pay a dividend to their policy holders. In making comparisons, you have to estimate the probable size of this dividend; this is difficult sometimes—particularly in the case of life insurance contracts which extend over a number of years.

The cost which must be charged by an insurer depends upon its expenses and losses, which in turn depend upon its efficiency as a business firm and upon the care with which it selects those it insures. Some insurers offer a low premium, but their underwriting standards are high and many applicants for coverage may not qualify. Care should be taken to avoid an insurer which offers a low premium when this premium is made possible by:

1. An unduly strict claims settlement policy.
2. The setting aside of inadequate loss reserves.
3. Low commissions so that the agent is in no position to render the quality and quantity of service you need and have a right to expect.

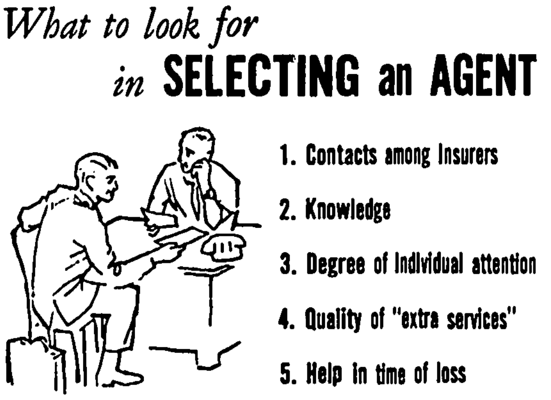
It is difficult to obtain a valid comparison of insurance costs, but you may sometimes obtain assistance from brokers or agents or independent insurance advisers. A careful cost analysis is well worth the time, trouble, and cost it involves.

Selecting an Agent

The small-business man should select his insurance agent in a manner similar to the way in which he selects other professional personnel who provide him with services. You should decide which qualifications are important and make inquiries among business friends and others who have had experience with different agents. Specifically, the following criteria can profitably be used in making comparisons:

1. *Contacts among insurers.* Are the agent's contacts wide enough to supply all the coverage you need at reasonable prices and without undue delays? In other words, can he obtain the insurance you require even for unusual exposures or unusual risks? Is he sufficiently familiar with the underwriting requirements of his insurers to avoid writing insurance for which you might not qualify and which would be canceled, causing needless expense and delays?

2. *Knowledge.* Is the agent known as a competent professional person, or as a "back slapper" who keeps his customers by "being a good Joe?" What is his experience and educational background? Can he answer questions about insurance correctly, confidently, and quickly? Is he sufficiently interested in his work to have acquired professional designations, such as C.P.C.U. or C.L.U.? (C.P.C.U. stands for Chartered Property Casualty Underwriter, a designation awarded by the American Institute for Property and Liability Underwriters, Inc., Bryn Mawr, Pa. C.L.U. stands for Chartered Life Underwriter, a designation awarded by the American College of Life Underwriters, Bryn Mawr, Pa. These two designations are awarded after the agent has passed five examinations, each requiring about 1 year of study.)



Visual No. 12—4

3. *Degree of individual attention.* Will the agent devote enough time to your individual problems to justify his commission?

4. *Quality of "extra services."* Is the agent able and willing to survey the exposures to loss which you face; to recommend what constitutes an adequate insurance program and recommend how you can prevent or control losses; to offer you alternative methods of insurance with recommendations of the advantages and disadvantages of each? Is he willing to provide such services at no extra cost?

5. *Help in time of loss.* Does the agent have the reputation of serving his clients well in time of loss? Have his other clients suffered uninsured losses, or have they failed to collect all losses easily and quickly because of his fault?

If you will spend the time to investigate thoroughly the insurance companies and agents available to you, you can be better assured of getting your money's worth from your insurance premium dollars.

TYPES OF COVERAGE

In planning their insurance programs, many small businessmen are confused by the sheer numbers of policies available and the many complexities involved in understanding them. They find that even the so-called "package" policies are actually many-sided agreements. Here are some of the basic insurance contracts that you may find useful.

Fire Insurance

Fire insurance is standardized throughout the United States. The basic policy is nearly identical in every State. The standard fire policy contains (1) an insuring clause; (2) 165 lines of stipulations and conditions that govern both your basic insurance contract and the additions—called extensions or endorsements—that are commonly attached to the basic policy; and (3) an attachment, known as *the form*, which describes the property being insured. (The Standard Form is reproduced as Handout No. 12–1.)

Perils Covered and Excluded. The standard fire policy, excluding any endorsements, insures you for only three perils: fire, lightning, and losses to goods temporarily removed from your premises because of a fire. You must pay for any additional perils by adding extensions to the basic policy.

The policy excludes theft, actions resulting from war or orders of civil authority, and negligence by the insured in using all reasonable means to save property after a loss. Coverage is suspended (1) if the hazard to your business is increased by any means within your control or knowledge; (2) if your property is vacant for an extended period; or (3) if an explosion or riot occurs, unless fire results (and then only the loss from such a fire is covered). Thus the policy suspends your coverage if you increase the hazard by running a dry-cleaning plant in your basement or if you change the basic nature of your business to one more hazardous.

Property Covered and Excluded. Property insured under the standard fire policy is listed both in the insuring clause and in the attached form. The policy excludes

property losses such as accounts, bills, currency, deeds, money or securities, and, unless specific endorsement is made, bullion and manuscripts. The form provides more specific information on insured property—indicating the extent of coverage on contents, foundations, trees, plants, shrubs, outbuildings, fences, walls, and other types of property. It also is used to add new perils to those covered by the basic contract.

Losses Excluded. In certain instances, even though an insured peril occurs, other resulting losses are either excluded altogether or limited. For example, the policy pays no indemnity for profits lost because of a fire. To cover such losses, you must carry business interruption insurance. We will come to this later. Losses arising solely from temperature change may be excluded; and those resulting from increased cost of repair or reconstruction made necessary by building codes are excluded. Losses to trees, shrubs, plants, and lawns are commonly limited to 5 percent of the basic policy amount.

Terms of Coverage. The most common term is 3 years. The insurer may cancel the policy for any reason upon 5-days notice. In such a case, any advance premium you have paid must be refunded on a pro rata basis, that is, in proportion to the unexpired term of the policy. *You* may cancel your policy at any time, without previous notice.

Extended Coverage. Most business firms find it necessary to supplement their basic fire insurance policy with an extended coverage endorsement. This does not add to the face amount of the standard fire policy; it merely extends the perils covered by the policy—naming windstorm, hail, explosion, riot, aircraft damage, vehicle damage, and smoke damage. The endorsement further defines and limits each of these perils.

General Liability Insurance

In conducting your business, you are subject to the rules of common and statutory law governing negligence to customers, employees, and anyone you do business with. Negligence may be defined as failure to exercise the degree of care required under the circumstances. For example, your firm is expected to maintain a safe place for customers to enter. If one of your customers falls on a slippery floor, you may be held liable for damages even though you had posted signs warning of danger. It is not a defense to say that your omitting to exercise due care was unintentional.

Failure of a small-business man to recognize the danger he faces by not carrying liability insurance can be one of the most serious errors in business management. One liability judgment could easily wipe out the entire assets of your firm and cause its liquidation. Judgments running into many thousands of dollars are common.

Because of the courts' severe attitude toward negligence liability, business firms have sought protection against the consequences of accidents arising within their operations. The many liability policies available have certain elements in common.

Coverage. Most liability policies will pay the following types of losses:

1. Liability judgments or other sums which you become legally obligated to pay because of bodily injury or damage to property of others that you cause accidentally;
2. Expenses you incur for whatever immediate medical and surgical relief to others is necessary at the time of an accident;
3. Costs of defending suits alleging bodily injury or property damage, even if such suits are without any real basis;
4. Your expenses in the investigation, defense, or settlement of an accident; and
5. The cost of any court bonds or interest levied on judgment accruing during an appeal period.

Thus you can obtain in one policy the assurance that the insurer (subject to policy limits) will bear all the expense and trouble of settling a liability suit. Many consider that having an insurer who will handle "nuisance suits" is in itself worth the cost of protection. With such protection, all you have to do is notify the insurer of your loss and cooperate with it in settling claims.

Exclusions. Most liability policies contain certain exclusions: (1) obligations under workmen's compensation laws (this peril is covered by workmen's compensation insurance, which we will discuss later); (2) damage to property of others which is in your care, custody, and control (this exclusion is sometimes eliminated by payment of an extra premium); and (3) liability resulting from blasting operations, from war, from the operation of State liquor laws, and from mishaps involving nuclear energy.

Limitations. Liability policies limit payments in several ways. The comprehensive general liability policy contains a limit per person and a limit per accident. For example, a contract may specify that in any one accident it will pay $100,000 per person injured, or a total of $300,000. Thus if two persons injured in a single accident are awarded judgments of $150,000 each, the policy will pay a total of only $200,000 because of the limit of $100,000 per person. Other policies may have a single limit applying to both bodily injury and property damage.

Automobile Liability Insurance

The basic principles of liability insurance apply to the liability the small-business man may incur in owning and maintaining or using an automobile.

Business firms are often legally liable for the use of trucks and passenger cars even though they do not own any. This happens when an employee or a subcontractor uses his own car on behalf of the employer. You are usually liable for an accident that occurs when your employees use rented or leased vehicles, or when an employee is operating a car belonging to customers. Various kinds of automobile liability policies provide protection for specific business uses.

Automobile Physical Damage Insurance

Almost all automobile owners carry insurance for damages from collision, fire, theft, and other physical perils. Insurance for physical damage is of several kinds. You can usually insure collision damage separately from other types of losses. You can insure all types of physical loss *except collision* by taking out a "comprehensive" policy. It excludes only (1) losses from wear and tear; (2) loss to tires (unless owing to fire, malicious mischief, or vandalism, or arising from a collision); (3) loss from radioactive contamination; and (4) loss from freezing or from mechanical or electrical breakdown. If any of these losses, except radioactive contamination, result from theft, you *are* covered, however.

If you don't want to buy automobile comprehensive insurance, you can cover separate perils. For example, you can buy fire and theft insurance at rates somewhat below those for comprehensive insurance. Theft insurance not only covers loss of your car by theft, including all damage done by thieves if the car is later recovered, but also pays you $10 per day for loss of use, subject to an aggregate limit of $300.

Workmen's Compensation and Employer Liability Insurance

Common law requires that an employer (1) provide his employees a safe place to work; (2) hire competent fellow employees; (3) provide safe tools; and (4) warn his employees of any existing danger. If he fails in these duties, he is liable, under both common law and workmen's compensation laws, for damage suits brought by an employee. Every employer thus needs protection for both kinds of liability.

Coverage. Under a workmen's compensation and employer's liability policy, the insurer pays all sums you are legally obligated to pay because of your common law liability; and it agrees to pay all compensation and other benefits that the applicable workmen's compensation law requires you to provide.

State laws determine the kind of benefits payable under workmen's compensation policies. The insurer does not determine the level or type of benefits, Most such laws provide medical care to the injured workman; lump sums for dismemberment and death; benefits for disablements by occupational disease; and

income payments for a disabled worker or his dependents. In some instances, income payments may last as long as the worker is disabled, even if it is for life.

Workmen's compensation laws do not cover all workers. In many States the laws exempt employers having only a few workers—four or less, for example. In about half the States, the employer has the option of covering his workers; if he does not, a worker may bring legal action for damages. Even in the States where coverage is compulsory, the laws do not cover all types of employment. Often excluded are agricultural, domestic, and casual labor. Finally, some States do not require coverage of an employer's workers located in another State. However a policy can have an endorsement that covers workers no matter where located.

Fidelity Bonds

Each year, thefts by employees probably amount to several times the loss from burglary, robbery, and larceny. Embezzlers often steal small amounts over a period of years, eventually draining enormous sums from their employers. Many times, discovery of embezzlement is concealed because of the presumed bad publicity among customers or creditors. Furthermore, less than 10 percent of such loss is insured. The small-business man, particularly, should consider the use of fidelity bonds to protect himself against this unpredictable hazard.

Crime Insurance

To most businessmen, crime insurance is the least familiar of the various types of insurance. It protects you against criminal activities committed by persons not connected with the business. There are no comprehensive or accurate data on the exact size of business losses from criminal acts; but available figures do suggest that they equal or exceed all property losses from fire each year. Thus the peril of crime to your firm is very serious. In many instances, burglarized or robbed firms unprotected by insurance have had no alternative but liquidation.

Crime insurance rates are generally high because of the considerable hazards attached to the perils covered. Rates depend on territory, number of watchmen, kind of loss prevention measures, type of safe and burglar alarm system, number of locations exposed, and type of business. Retail drug stores, for example, are considered less hazardous than grocery stores.

Burglary Insurance. Burglary insurance, covering safes and inventoried merchandise, is your basic protection against crime loss from "outsiders."

Robbery Insurance. Robbery insurance protects you from loss of property, money, and securities by robbery either on or off your premises. Robbery is defined as taking property from a person in charge of it by force or threat of violence.

Comprehensive Crime Policies. Certain comprehensive contracts cover not only burglary and robbery, but also other types of theft loss, destruction, or disappearance of property. Other comprehensive policies cover losses from forgery and counterfeiting.

Other Consequential Loss Policies. Even if their physical plants are destroyed, some firms (such as laundries, dairies, some retail businesses, and others) often find it possible to carry on by renting other quarters or leasing equipment belonging to others. A special type of consequential damage insurance, known as *extra expense insurance*, pays for the unexpected added expenses incurred in such situations.

Another type of policy, *contingent business interruption insurance*, covers your losses when your business suffers because an important supplier or customer's plant is damaged or destroyed by fire or other peril. The regular business interruption contract does not cover this kind of loss.

Power Plant Insurance

Power plant insurance, sometimes called boiler and machinery insurance, protects you against losses caused by explosions of furnaces, steam boilers, engines, and electrical equipment.

Glass Insurance

Insurance against the peril of glass loss has increased in recent years. Property covered includes plate glass windows, glass signs, motion picture screens, glass bricks, glass doors, showcases, countertops, and insulated glass panels.

BUSINESS LIFE INSURANCE

There are, of course, group life insurance and health insurance policies that a business can buy, or help buy, for their employees. Policies of this type improve workers' morale; and, in these days of intense competition for good employees, you may have to offer such fringe benefits to get the people you want. But these policies are basically designed more for the benefit of the employees themselves rather than the business, so we will consider a discussion of employee group insurance to be outside the scope of this presentation.

However, life and health insurance can be used in small business firms not only to benefit employees, but also to indemnify the firm when a key man is ill or dies.

Storekeeper's Burglary and Robbery Policy. A commonly used contract known as the storekeeper's burglary and robbery policy is designed specifically for small-business men. It covers up to $250 of loss for each of the following: outside robbery, inside robbery, stock burglary, safe burglary, kidnaping of the owner, burglary from the home of a custodian, and property damage by burglary or robbery.

All-Risk Physical Damage Contracts

After World War II, fire insurers developed contracts which offered "all-risk" and "multiple-line" coverage on property, subject to listed exclusions and limitations. This type of insurance offers considerably improved protection to the typical purchaser of fire insurance and related lines. All-risk policies cover all perils except those specifically excluded by name. Multiple-line policies list a much wider variety of perils covered than does the standard policy.

Business Interruption Insurance

Indirect or "consequential" losses are frequently even more severe in their eventual cost to the businessman than are direct losses from such perils as fire. Consider what can happen to you if you are forced to shut down your plant or store for 2 or 3 months following a serious fire. You may have full insurance on losses to raw materials, goods in process, finished goods, furniture and fixtures, and machinery and buildings. But while rebuilding, you must continue to pay salaries of key employees and such scheduled expenses as taxes, interest, depreciation, and utilities. Without earnings from production and sales, you would probably be sorely pressed. Business interruption insurance (in the form of an endorsement attached to the standard fire policy) was developed for this very kind of situation. Every small-business man should be familiar with the type of protection it offers him.

Key man coverage. Losses of key personnel are among the most serious setbacks a firm can have—particularly when the major asset of a firm, especially a small one, is the skills and training of its managers.

When deciding to insure such loss, a businessman must determine how much coverage he wants to carry. One sound approach is to estimate carefully the profit accounted for by the key man and to capitalize this sum at some appropriate figure. A firm also wants to insure the extra expenses which a key man's death would cause such as fees to manpower recruiting agencies, training costs of the new employee, and lost sales to important customers.

Business owners' insurance. Insurance for the protection of owners of a business is of two major types: (1) policies that protect an owner or his dependents against the

losses from premature death, disability, or medical expense; and (2) policies designed to assure the continuation of a business following the premature death of an owner.

Business continuation life insurance. Very frequently, serious problems result from the death of an owner of a sole proprietorship, a partner in a partnership, or a stockholder in a closely held corporation. Too often, no plans exist to solve such problems, and needless losses and controversies result. Advance planning—involving the combined talents of attorneys, trust officers, life insurance men, accountants, and others—almost always centers around providing ample cash and a plan for its use. Life insurance, where feasible is often the most acceptable and economical method of providing the cash; and a trust agreement, coupled with a purchase and sale plan, is the best way of providing for its effective use.

Ample supplies of ready cash can be used to retire the interest of a partner or sole proprietor or to repurchase the stock of a stockholder in a closely held corporation. The business can then continue without interference from heirs of the deceased, without danger of controlling interest being sold to a competitor, without the danger of loss of credit, and without the necessity of selling fixed assets to pay estate and other taxes. Usually, such life insurance can be bought on a cross-purchase plan or on an entity plan.

Under a cross-purchase plan, partners or stockholders buy sufficient insurance on each other's lives to retire each other's interest in case of death. Under the entity plan, a firm buys the necessary insurance on the lives of its principal owners. The business owns the policies and is their beneficiary.

If your particular insurance needs are not covered by the basic policies we have discussed, perhaps you can have one tailor-made to fit your situation. Many businessmen do not know that insurers can often design a special contract to cover a particular risk if a standard policy is not available. In fact, some of the insurance policies now in wide use were developed in just this way.

The important thing for you to do is to evaluate your risks, review your present coverage, and take the necessary action that will assure you of the protection you need.

NOTE: The source for the preceding sections is Mark R. Greene's *Insurance and Risk Management for Small Business* (SBA's Small Business Management Series No. 30).

MANAGEMENT SUCCESSION

There is another risk that insurance cannot adequately protect you against, and that is the risk associated with management succession and the continuity of the business. Even "key man" insurance cannot fully protect your business when you or one of your top men die or are disabled. What is needed is careful planning for management succession.

The *Small Business Reporter*, published by the Small Business Advisory Service of the Bank of America, made this observation in its November 1961 issue:

> "If a business lives on after the death, disability, or retirement of the owner, it can be assumed that he did some management succession planning. His preparations preserved his family estate, the jobs, economic usefulness, and social values related to his business, The small business unit that might have gradually disappeared has been given a new lease on life—all due to forethought.
>
> "Do many small business proprietors, partners, and owners of closely held corporations engage in management succession planning? Not nearly enough. . . .
>
> "Typically, the owner of a small business *is* the business. He has spent his entire lifetime building it and the very nature of his struggle has made him aggressive and self-sufficient.
>
> "When he makes no arrangement for his successor, it is because he forgets or puts it off, or doesn't like to face the fact that he can't go on forever. The businessman can usually be proud of what he has done to provide a better life for his family and greater opportunities for employment in the community. But he fails in his continued responsibility to them if he disregards the effect that lack of planned management succession can have. . . ."

The *Reporter* goes on to indicate that management of small firms seem to operate on the theory that their workload will not justify adding a potential successor to the payroll, and on the implicit faith that the problems of management replacement can be handled promptly whenever the need should arise.

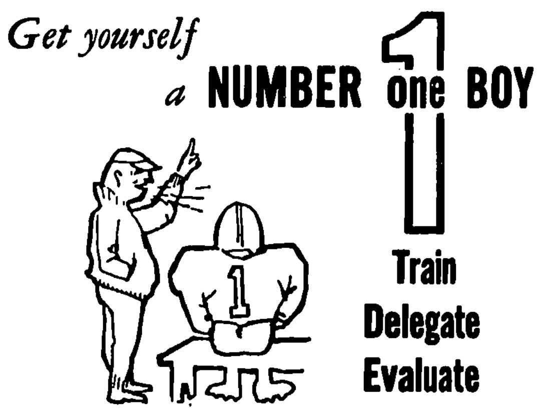
Harry M. Meacham, a now retired Dun & Bradstreet executive, time and time again urged small business owners to get themselves "A Number-One Boy"—someone to take over in time of emergency.

What would happen to *your* business—and it follows to your family and estate—if you suffered a sharp pain in your chest, and couldn't open the store tomorrow? Who would take over?

Your son, you say! Fine, but what does he know about the business? Several years ago, at a management course such as this in the Valley of Virginia, a young man approached the rostrum during a break with "worry" written all over his face.

"My problem," he said, "is my father. I'm supposed to take over the store eventually, but I don't even have a key to the place. I've never seen his financial statements. I've never been permitted to buy so much as a keg of nails."

Failure to bring young people along in the business—which is, actually, failure to plan for the future—is one of the fundamental weaknesses of small business management. And it is also one of the important reasons why many remain small—or disappear.



Visual No. 12—5

A few years ago Roland Christensen wrote a book, *Management Succession in Small and Growing Businesses*. This volume grew out of hundreds of interviews with small enterprisers all over the country. Bank and trust officers interviewed estimated that from 70 to 90 percent of the small businesses with which they were familiar had failed to look ahead and prepare for management succession. This can have very serious effects.

Effects of Not Planning for Management Succession

- The business may legally come to an end and have to be sold at a forced-sale price.
- There may be inadequate funds to pay estate taxes and administrative expenses.
- Lack of capable managers to carry on may result in great operating losses and disrupt the operation of the business for a considerable period.
- People the owner would like to see carry on the business will liquidate rather than retain it.

- Partners, stockholders, or employees may not have the ready funds to buy the available share of the business, even if they want to.
- Unqualified heirs may try to run the business, and ruin it and its value in the process.

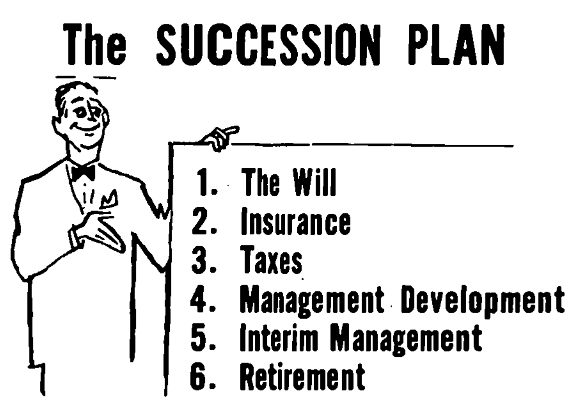
These are just some of the possibilities—enough to indicate the vital importance of planning ahead for the problem of succession. Many small business owners have made adequate provisions for the eventuality of their death or disablement. There are many courses of action open. The wise businessman will do well to thoughtfully consider a number of procedures which have proved advantageous to others.

The questions on a handout sheet you will be given are some of the important ones to think about when making plans for management succession. A qualified advisor can probably add more.

Now, let's look at factors to consider in the succession plan.

The Succession Plan

The thoughtful businessman considering these and other questions concerning management and ownership succession might well draw up a plan taking into account all the important factors involved. These factors—legal, tax, insurance, business policy—are highly technical and few businessmen can prepare such plans themselves. To find the best course of action he should consult some or all of the following: attorneys with estate planning experience, bankers, trust experts, certified public accountants, management consultants, investment counsellors, and insurance specialists.



Visual No. 12—6

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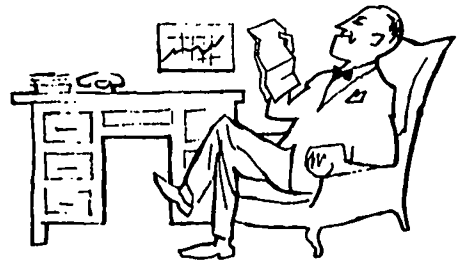
The Will. When the owner has formulated a general plan for the future of his business, he should consult his attorney. It is essential to have a properly executed, up-to-date will, giving authority to the executors to carry out the provisions.

The SUCCESSION PLAN (1)

The Will



Visual No. 12—7

Insurance. Insurance specialists will advise on the type of insurance to meet the individual requirement of the business concerned.

The SUCCESSION PLAN (2)

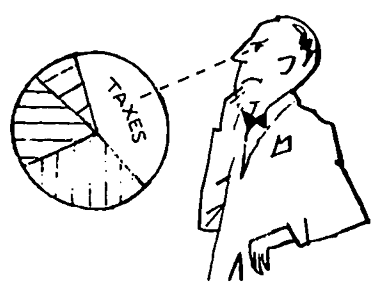
Insurance

Visual No. 12—8

Tax Implications. If the owner has the bulk of his estate value tied up as an investment in his business, the high estate tax assessment may force liquidation.

The SUCCESSION PLAN (3)

Taxes



Visual No. 12—9

A business continuation arrangement, developed upon the advice of professional counsel, may be used to provide a method of predetermining the value of the business for death tax purposes.

It is also imperative to plan for income tax. To obtain adequate protection, a tax expert and a trust officer should be consulted at least ten years prior to the owner's expected retirement date.

Management Development. If the owner has decided the business is to continue after he leaves, he will need to provide training for some person or persons to prepare them for top management responsibility. This can range from training a close relative in the smaller business, to the creation of a capable management group in the larger company.

The SUCCESSION PLAN (4)

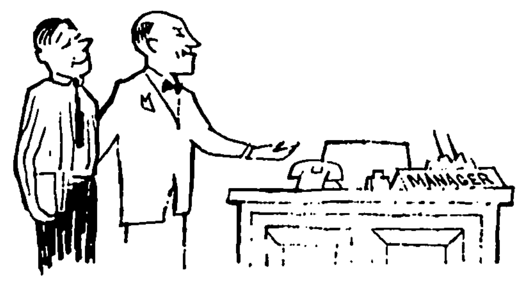
Management Development

Visual No. 12—10

Interim Management. When a definite successor has not been agreed upon, the owner should include in his plan a provision for interim management, making the necessary authorization in his will. This means that in case of the owner's sudden death, someone is named to take over the daily running of the business until more permanent arrangements can be made. The need for a new manager is then not so urgent, and an unhurried, duly considered choice can be made.

The SUCCESSION PLAN (5)

Interim Management

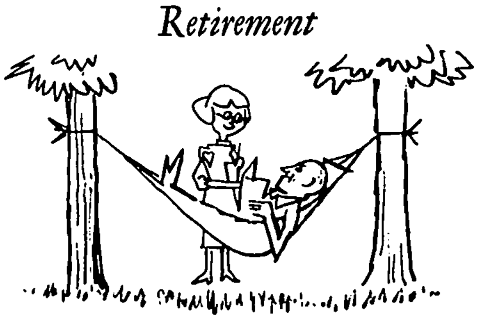


Visual No. 12—11

Retirement. Often the owner of a small business is unwilling to retire. He wants to go on managing his business, to the point when he begins to lose his grip. He can eliminate many problems if he acknowledges the likelihood of his situation and includes in his succession plan a retirement program, both for himself and for other members of management. In this way the members of the management team can step down gracefully when they are scheduled to retire.

The SUCCESSION PLAN (6)

Retirement



Visual No. 12—12

The Succession Plan for Different Types of Ownership

The Sole Proprietorship

This type of business organization is usually small, and the owner constitutes virtually the whole management. In this case the owner can consider the possibility of his wife taking over, if she is so inclined, but he will have to give her as much training as possible. He can do this by (a) explaining to her the day-to-day running of the business, (b) talking over his problems with her, (c) bringing her in when personnel are temporarily absent or having her work regularly in the business, (d) instructing her in management principles, (e) informing her of the business plans and policies, and (f) sharing financial information with her. The owner should also consider the advantages of developing key employees or outsiders, so that his wife will not be required to assume the entire burden of management.

Proprietorship insurance on the life of the owner can provide ready funds to meet debts or taxes and tide over the business in its transition period.

The Partnership

Plans for the continuation of the partnership business might take one or more of the following forms, all of which require an agreement obligating the heirs of the deceased partner in some way:

1. A new firm with heirs of the deceased as partner-managers.

2. A new firm with outside purchasers of the partner's interest assuming management functions.

3. A continuation of the business with the deceased or retired partner's interest being purchased by the remaining partners.

A buy-and-sell agreement provides for the buying out of a specified part of a partner's share on retirement or at death (at a prefixed valuation). This agreement can be insured to provide the funds to carry it out in the case of death.

The Corporation

Management Development. (The remarks under this heading also apply to larger partnerships and sole proprietorships.) An essential function of sound management is to achieve a balanced executive group, both in skills and age groups. When management members grow old together, they tend to retire within a short time of each other and a large management gap is created. Similarly, when members of the management group have been managers in name only and have had no experience in major decision making, they will lack the requisite management skills to take over when the need suddenly arises. If, to prevent this, it is necessary to enlarge the management group by promotion from within or the hiring of new staff, the top management should not hesitate to do this. Although, as already mentioned, the small business cannot use all the training techniques of large companies, there are plenty of opportunities and methods available to develop potential managers.

Training of younger men possessing adaptability, intelligence, and drive should be undertaken, even if there are insufficient positions for all to receive promotion to management posts.

Outside Counsel and Advice. Many small businesses benefit by having outsiders on their board of directors. The outside group can render valuable aid by urging the owner to make plans for his succession. When necessary, they can aid in building up a strong management organization, they can make recommendations as to the actual successor, and they can give advice and help to the new manager when he takes over. They can also assist in the formation of company policies.

Stock Sale and Purchase Agreement. Such an agreement, funded by life insurance, can provide for the repurchase by the corporation of a shareholder's stock at his death or at the time he wishes to sell. This method can be used to prevent disruptive changes in ownership, maintain continuation of management and opera-

tion at the time a principal stockholder dies, and keep the corporation in close ownership. It also quickly gives the deceased shareholder's heirs full value for his interest.

The Family Business

Ownership Succession. In the family-owned corporation, the owner/manager should understand that the long range continuance of the business can be endangered by keeping both top management and ownership in the family, if this could mean having children or close relatives taking over on the basis of majority ownership rather than experience and ability. In any case, the present day tax situation and the splintering of stockholdings as they are passed down into a larger family group will usually bring about separation of ownership and management over a period of years.

There are two other precautions which can be taken, if necessary, to prevent an adverse family influence on the company:

1. If the owner wishes a particular relative to eventually be his successor, both as majority stockholder and top manager, he can arrange for a small holding of stock to be given to the relative on the owner's death. Further stock can then be turned over to him gradually, providing he shows the necessary ability (measured by the performance of the company).

2. If the owner wants ownership but not management control to remain with the family, he could consider the appointment of trustees to take over the voting rights of family stock beneficiaries.

Management Succession. There are outstanding examples of successful businesses in this country today, both large and small, where father has been succeeded by son. There have also been a great many business failures caused by the succession to top management positions of close relatives. There are both strengths and weaknesses involved where family members participate in the management of a business—family solidarity can be the very thing which makes a business successful. On the other hand, family feuds and disagreements can bring about its downfall. When relatives come into a business, and birth predetermines their rise to top management positions, they should still work their way up through the organization, be advanced on merit and receive an extensive overall training that will develop them into effective leaders.

THE LAST BEST CHANCE

While no man likes to consider his own death and the effect it will have on his family and business fortunes, death is still inevitable. While it cannot be avoided, its effect may be cushioned.

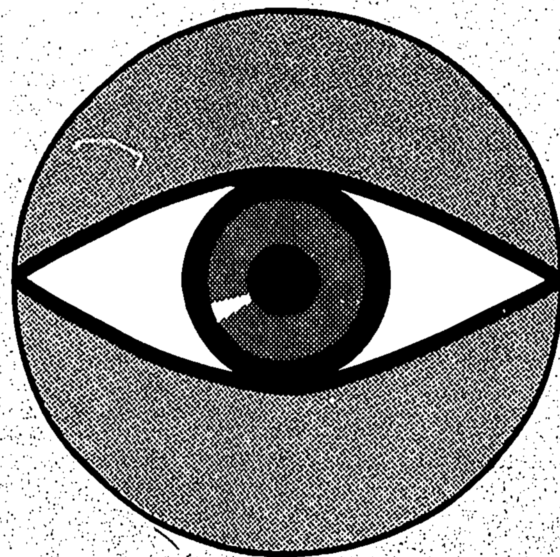
As pointed out above, preparations for orderly management succession, or the most advantageous handling of a business and personal estate, are not matters for the businessman to undertake entirely on his own.

But help is available.

There is just one requirement . . . a willingness to anticipate the burdens of death, and to seek help that will smooth the path of management and ownership succession, at the same time that it thoughtfully provides maximum benefits for the heirs.

The future has a habit of catching up with us before we know it. To be successful, you have to plan for the future before it is too late. A well-thought-out insurance program and a management succession plan are essential if you want to be satisfied with the future when it becomes the present.

NOTE: This section on management succession is based on the November 1961 issue of *The Small Business Reporter*, Bank of America, Small Business Advisory Service, San Francisco, Calif.



THE VISUAL AIDS

A What to Show

Section

The old Chinese proverb **"One See Worth Thousand Say"** is certainly borne out by experience in the fields of education and training at all levels.

The instructor who helps his participants **visualize** subject matter and ideas not only holds the group interest--he also stimulates thoughtful consideration and retention of the topic.

This section contains samples of visuals that are available for this subject. Each has been carefully coded and "keyed" into **The Lesson Plan** as outlined in this manual.

USE OF VISUAL AIDS

WHAT TO USE	WHEN AND HOW TO USE

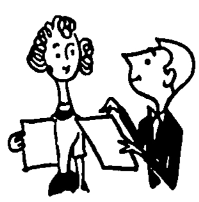
Chalkboard

Study and plan before a meeting what to put on the board and where to put it. Use it to present sketches, diagrams, outlines, definitions, key words, directions, record of class contributions, and summaries.
Suit material to board space.
Write plainly and quickly.
Keep wording simple.
Stand at one side of board while referring to material.
Talk to the group, not to the board.
Erase material no longer needed.

Posters, Charts, and Diagrams

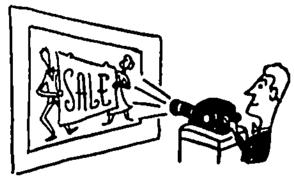
To arouse interest and attract attention; to show relationships and trends; to inspire group.
Use device large enough to be seen.
Post where everyone can see.
Present at right time.
Discuss information illustrated.

Hand-Out Materials



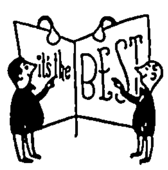
To present information uniform in character and as a guide to material covered; emphasize key points; arouse interest and discussion; review or summarize discussions; and serve as permanent reference.
Select to serve a definite purpose.
Introduce at right time.
Distribute in manner to convey its importance.
Direct members how to use.

Films and Film Strips



Present an overall view; introduce a new subject; emphasize specific aspects of a subject; arouse interest; summarize.
Select carefully to relate to the discussion and plan presentation. Arrange room and equipment for showing. Alert the audience for the showing or what will be seen. Run the film. Discuss the subject matter and summarize.

Samples, Forms, and Exhibits

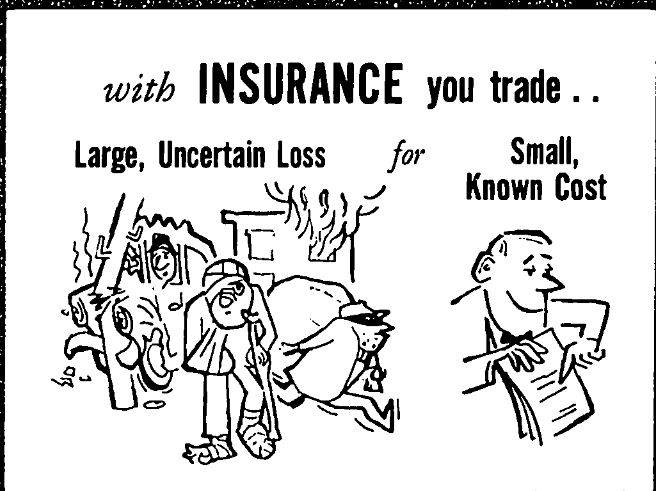


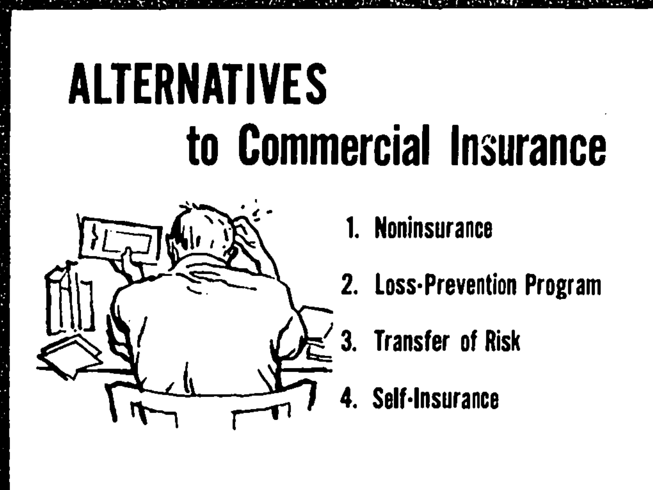
Keep subject matter practical; show development of a process; increase understanding.
Select only enough to illustrate, not confuse.
Pass around if necessary.
Take time to present clearly.
Comment when presenting.

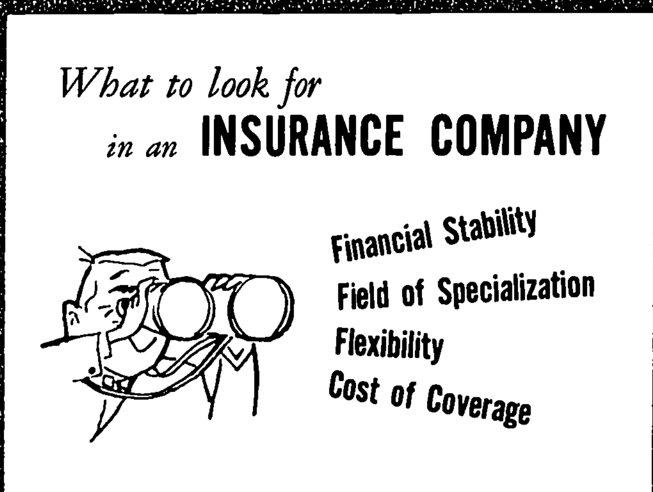
Pedestal Chart

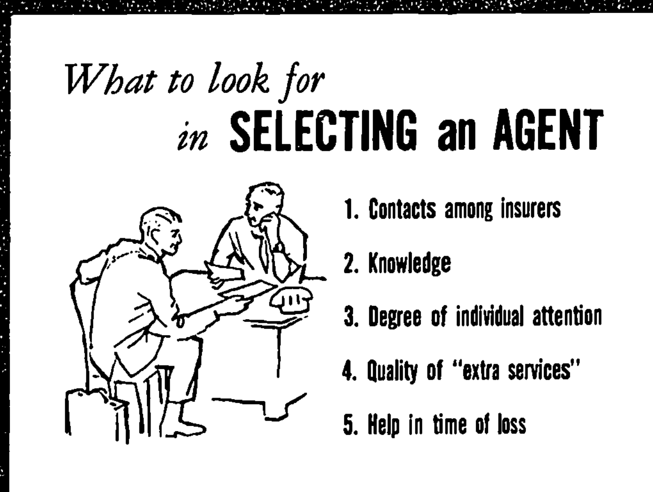
A pad of newsprint sheets or similar paper may be used for the same purposes as the chalkboard. Material recorded with chalk or crayon may be saved for future reference by the group or by the instructor.

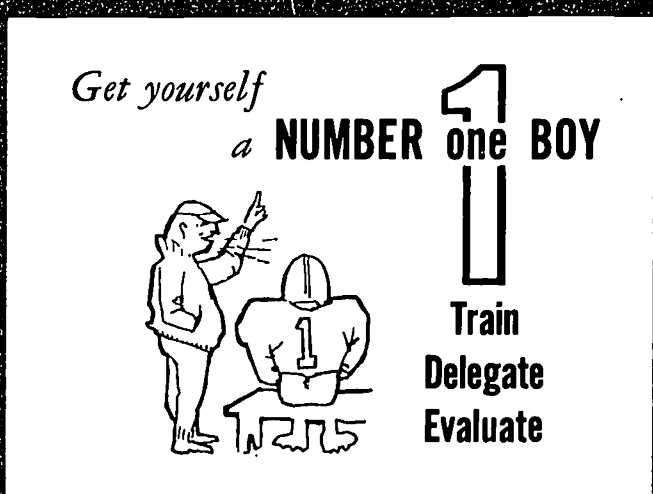
OVERHEAD PROJECTUALS

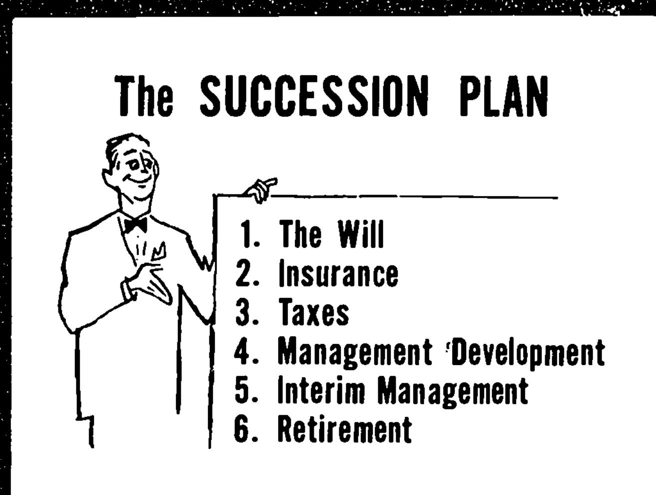












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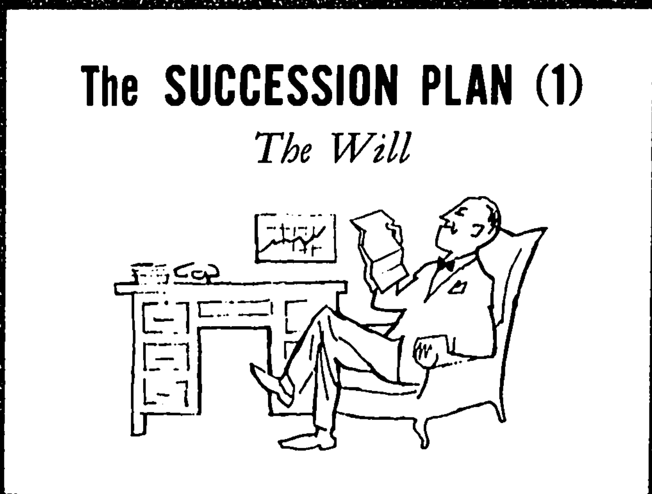
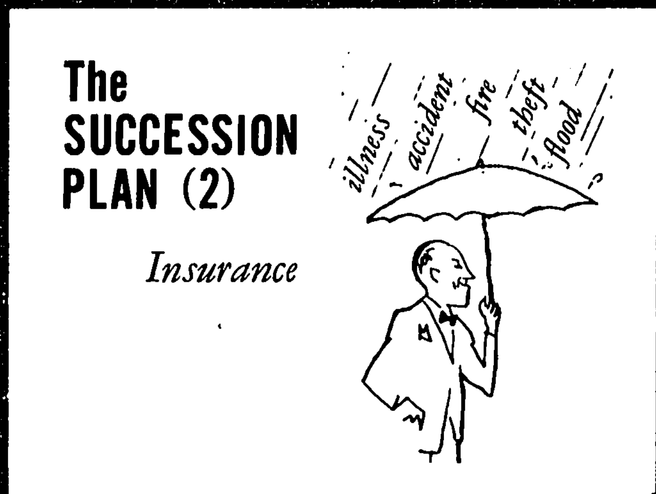
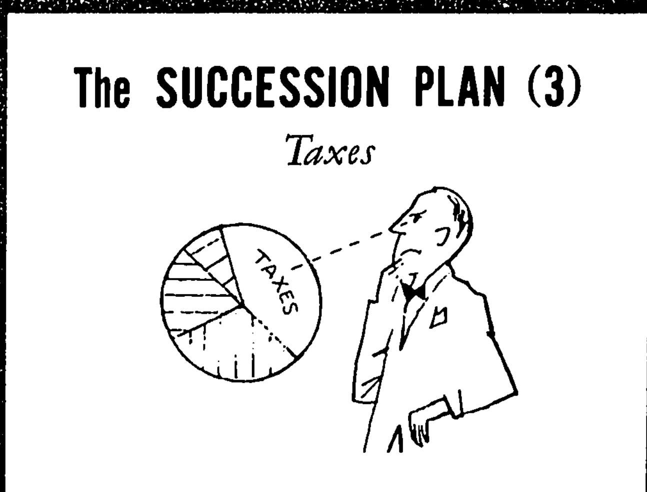
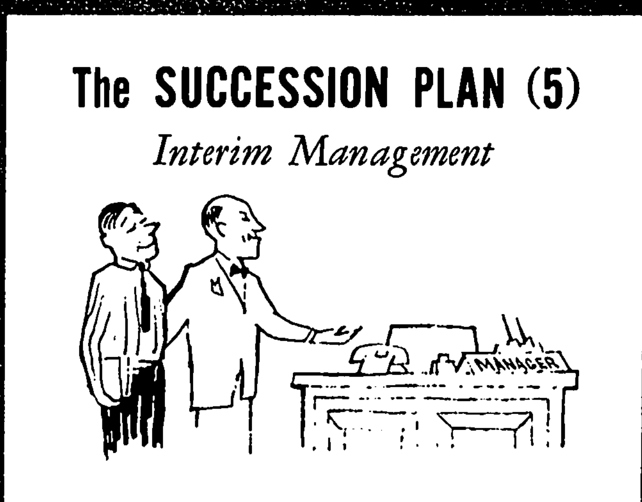
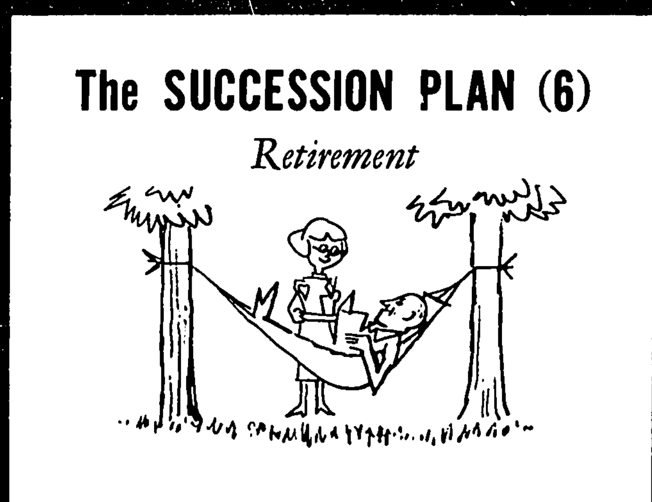










THE SUPPLY DEPARTMENT

Standard Fire Insurance Policy for Alabama, Alaska, Arizona, Arkansas, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maryland, Michigan, Mississippi, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin and Wyoming

No.

CAPITAL STOCK COMPANY

RENEWAL OF NUMBER

AUTHENTIC

SPACE FOR COMPANY NAME, INSIGNIA, AND LOCATION

Insured's Name and Mailing Address

SPACE FOR
PRODUCER'S NAME AND
MAILING ADDRESS

Inception (Mo. Day Yr.) Expiration (Mo. Day Yr.) Years

It is important that the written portions of all policies covering the same property read exactly alike. If they do not, they should be made uniform at once.

INSURANCE IS PROVIDED AGAINST ONLY THOSE PERILS AND FOR ONLY THOSE COVERAGES INDICATED BELOW BY A PREMIUM CHARGE AND AGAINST OTHER PERILS AND FOR OTHER COVERAGES ONLY WHEN ENDORSED HEREON OR ADDED HERETO.

AMOUNT	RATE	PREPAID TERM PREMIUM DUE AT INCEPTION	ANNUAL PAYMENT DUE UNDER DEF. PREM. PAY. PLAN	PERIL(S) Insured Against and Coverage(s) Provided (Insert Name of Each)
$	$	$	$	FIRE AND LIGHTNING
XXXXXXX	$	$	$	EXTENDED COVERAGE
	$	$	$	
	$	$	$	
$ TOTAL PREMIUM FOR POLICY TERM UNDER D. P. P. P.		TOTAL(S) $	$	

Item No.	Amount Fire or Fire and Extended Coverage, or Other Peril	Per Cent of Co-Insurance Applicable	DESCRIPTION AND LOCATION OF PROPERTY COVERED Show construction, type of roof and occupancy of building(s) covered or containing the property covered. If occupied as a dwelling state number of families.
1. -	$		

Subject to Form No(s). INSERT FORM NUMBER(S) AND EDITION DATE(S) **attached hereto.**

Mortgage Clause: Subject to the provisions of the mortgage clause attached hereto, loss, if any, on building items, shall be payable to:

INSERT NAME(S) OF MORTGAGEE(S) AND MAILING ADDRESS(ES)

Agency at

Countersignature Date

_______________________________ Agent

IN CONSIDERATION OF THE PROVISIONS AND STIPULATIONS HEREIN OR ADDED HERETO AND OF the premium above specified, this Company, for the term of *years specified above* from *inception date shown above* At Noon (Standard Time) to *expiration date shown above* At Noon (Standard Time) at location of property involved, to an amount not exceeding the amount(s) above specified, does insure *the insured named above* and legal representatives, to the extent of the actual cash value of the property at the time of loss, but not exceeding the amount which it would cost to repair or replace the property with material of like kind and quality within a reasonable time after such loss, without allowance for any increased cost of repair or reconstruction by reason of any ordinance or law regulating construction or repair, and without compensation for loss resulting from interruption of business or manufacture, nor in any event for more than the interest of the insured, against all **DIRECT LOSS BY FIRE, LIGHTNING AND BY REMOVAL FROM PREMISES ENDANGERED BY THE PERILS INSURED AGAINST IN THIS POLICY, EXCEPT AS HEREINAFTER PROVIDED,** to the property described herein while located or contained as described in this policy, or pro rata for five days at each proper place to which any of the property shall necessarily be removed for preservation from the perils insured against in this policy, but not elsewhere.

Assignment of this policy shall not be valid except with the written consent of this Company.

This policy is made and accepted subject to the foregoing provisions and stipulations and those hereinafter stated, which are hereby made a part of this policy, together with such other provisions, stipulations and agreements as may be added hereto, as provided in this policy.

Handout No. 12-1

Concealment, fraud. This entire policy shall be void if, whether before or after a loss, the insured has wilfully concealed or misrepresented any material fact or circumstance concerning this insurance or the subject thereof, or the interest of the insured therein, or in case of any fraud or false swearing by the insured relating thereto.

Uninsurable and excepted property. This policy shall not cover accounts, bills, currency, deeds, evidences of debt, money or securities; nor, unless specifically named hereon in writing, bullion or manuscripts.

Perils not included. This Company shall not be liable for loss by fire or other perils insured against in this policy caused, directly or indirectly, by: (a) enemy attack by armed forces, including action taken by military, naval or air forces in resisting an actual or an immediately impending enemy attack; (b) invasion; (c) insurrection; (d) rebellion; (e) revolution; (f) civil war; (g) usurped power; (h) order of any civil authority except acts of destruction at the time of and for the purpose of preventing the spread of fire, provided that such fire did not originate from any of the perils excluded by this policy; (i) neglect of the insured to use all reasonable means to save and preserve the property at and after a loss, or when the property is endangered by fire in neighboring premises; (j) nor shall this Company be liable for loss by theft.

Other Insurance. Other insurance may be prohibited or the amount of insurance may be limited by endorsement attached hereto.

Conditions suspending or restricting insurance. Unless otherwise provided in writing added hereto this Company shall not be liable for loss occurring

(a) while the hazard is increased by any means within the control or knowledge of the insured; or

(b) while a described building, whether intended for occupancy by owner or tenant, is vacant or unoccupied beyond a period of sixty consecutive days; or

(c) as a result of explosion or riot, unless fire ensue, and in that event for loss by fire only.

Other perils or subjects. Any other peril to be insured against or subject of insurance to be covered in this policy shall be by endorsement in writing hereon or added hereto.

Added provisions. The extent of the application of insurance under this policy and of the contribution to be made by this Company in case of loss, and any other provision or agreement not inconsistent with the provisions of this policy, may be provided for in writing added hereto, but no provision may be waived except such as by the terms of this policy is subject to change.

Waiver provisions. No permission affecting this insurance shall exist, or waiver of any provision be valid, unless granted herein or expressed in writing added hereto. No provision, stipulation or forfeiture shall be held to be waived by any requirement or proceeding on the part of this Company relating to appraisal or to any examination provided for herein.

Cancellation of policy. This policy shall be cancelled at any time at the request of the insured, in which case this Company shall, upon demand and surrender of this policy, refund the excess of paid premium above the customary short rates for the expired time. This policy may be cancelled at any time by this Company by giving to the insured a five days' written notice of cancellation with or without tender of the excess of paid premium above the pro rata premium for the expired time, which excess, if not tendered, shall be refunded on demand. Notice of cancellation shall state that said excess premium (if not tendered) will be refunded on demand.

Mortgagee interests and obligations. If loss hereunder is made payable, in whole or in part, to a designated mortgagee not named herein as the insured, such interest in this policy may be cancelled by giving to such mortgagee a ten days' written notice of cancellation.

If the insured fails to render proof of loss such mortgagee, upon notice, shall render proof of loss in the form herein specified within sixty (60) days thereafter and shall be subject to the provisions hereof relating to appraisal and time of payment and of bringing suit. If this Company shall claim that no liability existed as to the mortgagor or owner, it shall, to the extent of payment of loss to the mortgagee, be subrogated to all the mortgagee's rights of recovery, but without impairing mortgagee's right to sue; or it may pay off the mortgage debt and require an assignment thereof and of the mortgage. Other provisions relating to the interests and obligations of such mortgagee may be added hereto by agreement in writing.

Pro rata liability. This Company shall not be liable for a greater proportion of any loss than the amount hereby insured shall bear to the whole insurance covering the property against the peril involved, whether collectible or not.

Requirements in case loss occurs. The insured shall give immediate written notice to this Company of any loss, protect the property from further damage, forthwith separate the damaged and undamaged personal property, put it in the best possible order, furnish a complete inventory of the destroyed, damaged and undamaged property, showing in detail quantities, costs, actual cash value and amount of loss claimed; **and within sixty days after the loss, unless such time is extended in writing by this Company, the insured shall render to this Company a proof of loss,** signed and sworn to by the insured, stating the knowledge and belief of the insured as to the following: the time and origin of the loss, the interest of the insured and of all others in the property, the actual cash value of each item thereof and the amount of loss thereto, all encumbrances thereon, all other contracts of insurance, whether valid or not, covering any of said property, any changes in the title, use, occupation, location, possession or exposures of said property since the issuing of this policy, by whom and for what purpose any building herein described and the several parts thereof were occupied at the time of loss and whether or not it then stood on leased ground, and shall furnish a copy of all the descriptions and schedules in all policies and, if required, verified plans and specifications of any building, fixtures or machinery destroyed or damaged. The insured, as often as may be reasonably required, shall exhibit to any person designated by this Company all that remains of any property herein described, and submit to examinations under oath by any person named by this Company, and subscribe the same; and, as often as may be reasonably required, shall produce for examination all books of account, bills, invoices and other vouchers, or certified copies thereof if originals be lost, at such reasonable time and place as may be designated by this Company or its representative, and shall permit extracts and copies thereof to be made.

Appraisal. In case the insured and this Company shall fail to agree as to the actual cash value or the amount of loss, then, on the written demand of either, each shall select a competent and disinterested appraiser and notify the other of the appraiser selected within twenty days of such demand. The appraisers shall first select a competent and disinterested umpire; and failing for fifteen days to agree upon such umpire, then, on request of the insured or this Company, such umpire shall be selected by a judge of a court of record in the state in which the property covered is located. The appraisers shall then appraise the loss, stating separately actual cash value and loss to each item; and, failing to agree, shall submit their differences, only, to the umpire. An award in writing, so itemized, of any two when filed with this Company shall determine the amount of actual cash value and loss. Each appraiser shall be paid by the party selecting him and the expenses of appraisal and umpire shall be paid by the parties equally.

Company's options. It shall be optional with this Company to take all, or any part, of the property at the agreed or appraised value, and also to repair, rebuild or replace the property destroyed or damaged with other of like kind and quality within a reasonable time, on giving notice of its intention so to do within thirty days after the receipt of the proof of loss herein required.

Abandonment. There can be no abandonment to this Company of any property.

When loss payable. The amount of loss for which this Company may be liable shall be payable sixty days after proof of loss, as herein provided, is received by this Company and ascertainment of the loss is made either by agreement between the insured and this Company expressed in writing or by the filing with this Company of an award as herein provided.

Suit. No suit or action on this policy for the recovery of any claim shall be sustainable in any court of law or equity unless all the requirements of this policy shall have been complied with, and unless commenced within twelve months next after inception of the loss.

Subrogation. This Company may require from the insured an assignment of all right of recovery against any party for loss to the extent that payment therefor is made by this Company.

IN WITNESS WHEREOF, this Company has executed and attested these presents; but this policy shall not be valid unless countersigned by the duly authorized Agent of this Company at the agency hereinbefore mentioned.

INSERT SIGNATURES AND TITLES OF PROPER OFFICERS

MAJOR TYPES OF INSURANCE

FIRE INSURANCE

GENERAL LIABILITY INSURANCE

AUTOMOBILE LIABILITY INSURANCE

AUTOMOBILE PHYSICAL DAMAGE INSURANCE

WORKMAN'S COMPENSATION

FIDELITY BONDS

CRIME INSURANCE

- Burglary Insurance
- Robbery Insurance
- Comprehensive Crime Policies

ALL-RISK CONTRACTS

BUSINESS INTERRUPTION INSURANCE

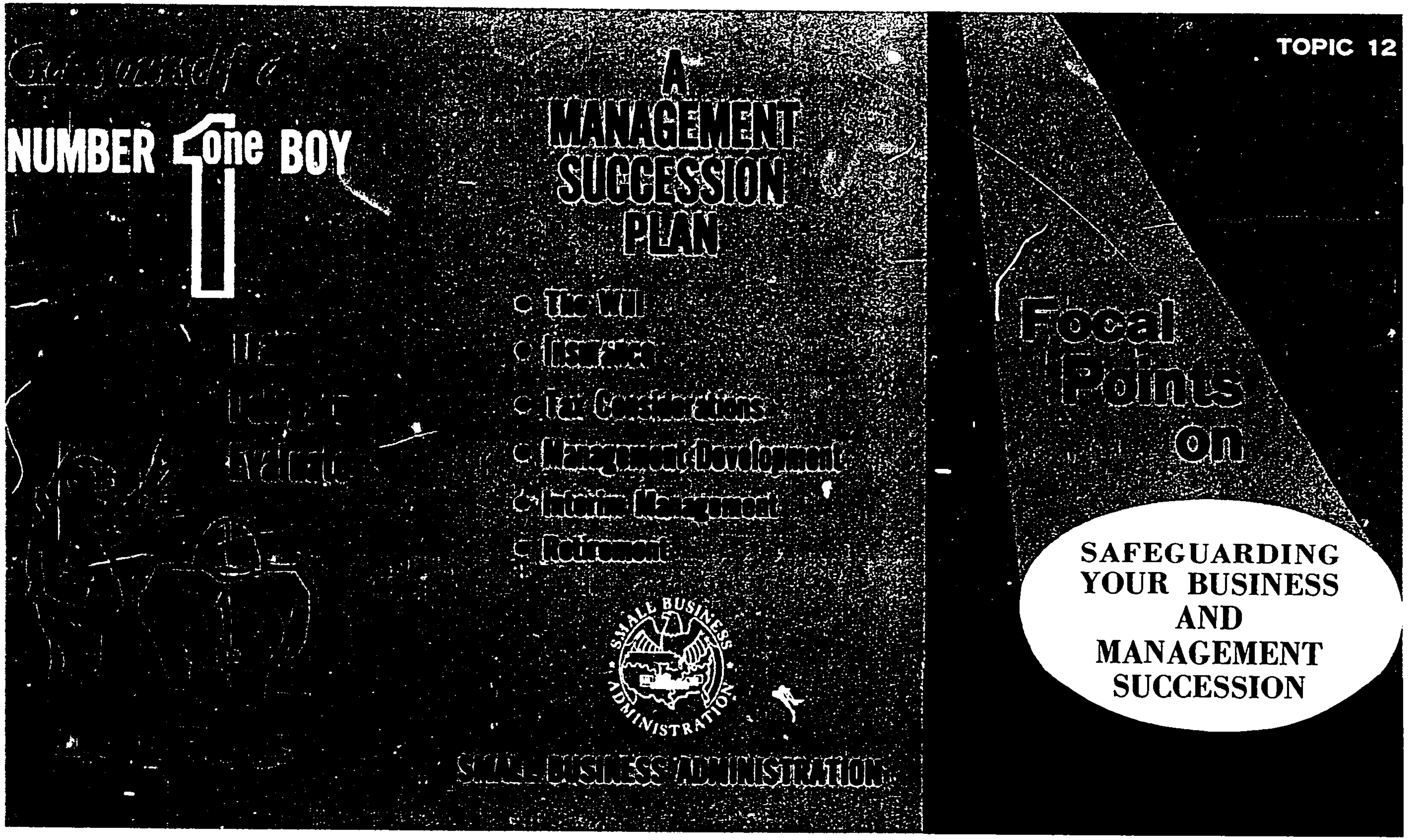
POWER PLANT INSURANCE

GLASS PLANT INSURANCE

BUSINESS LIFE INSURANCE

- Key Man Coverage
- Business Owner's Insurance
- Business Continuation Life Insurance

Handout No. 12-2



This page and the following illustrate a two-fold leaflet which summarizes the subject presentation. The leaflet is available in quantity from the nearest Small Business Administration office for distribution to participants in SBA-cosponsored administrative management courses.

What to look for in:

an INSURANCE COMPANY

1. Financial Stability
2. Field of Specialization
3. Flexibility
4. Cost of Coverage

an AGENT

1. Contacts among insurers
2. Knowledge
3. Individual attention
4. "Extra" services
5. Help in time of loss

MAJOR TYPES OF INSURANCE

Fire Insurance

Liability Insurance

Workmen's Compensation

Fidelity Bonds

Crime Insurance

All-Risk Contracts

Business Interruption Insurance

Power Plant Insurance

Glass Insurance

Business Life Insurance

ALTERNATIVES to COMMERCIAL INSURANCE

1. Noninsurance
2. Loss Prevention Program
3. Transfer of Risk
4. Self-Insurance

779-024 O—65——4

Questions to Consider in Planning for Management Succession

- What does the owner want to happen to his business—continuation, sale, or liquidation?
- What will happen to the business if no prior arrangements have been made?
- What will be the value of the business for estate tax purpose?
- Where will the funds come from to pay estate administration costs, estate taxes, and other debts?
- What effect may the different forms of business organization—sole proprietorship, partnership, corporation—have on the succession problem?
- Should the form of business organization be changed in the owner's lifetime?
- How will key business contacts—suppliers, customers, financial institutions—view the continuance of the business under unknown or unproven management?
- Will the sale or continuation value of the business be sufficient to provide satisfactory income for the owner's dependents?
- Who will run the business if it is continued?
- Is there a training program for successors?
- Are there qualified employees or family members ready to take over now—permanently or temporarily—if the need should suddenly arise?
- If it is planned to sell the business to employees, partners, or stockholders, will they have sufficient funds to acquire it?
- Should a trustee be appointed to run the business?
- How much will the business bring if sold?
- Who will sell it?
- Who will buy it?
- Can arrangements be made beforehand for an outside sale or merger to take place on the owner's death?
- How will the sale value of the business be affected, minus the presence and skill of the owner?
- Should arrangements be made for the business to be liquidated?

Handout No. 12–3

SMALL BUSINESS ADMINISTRATION

Management Aids FOR SMALL MANUFACTURERS

130

Washington 25, D.C.

October 1961

BUSINESS LIFE INSURANCE

Prepared by the Institute of Life Insurance,
New York, New York

WHAT IS BUSINESS LIFE INSURANCE?

Business life insurance is life insurance used to protect a business, or the family of a businessman, from the financial loss which results from the death of someone associated with the business. Many billions of dollars worth of this protection is now in force, giving assurance of business continuity to the firms and full value of the business equity to the family of the deceased.

There is no basic difference between business life insurance and the life insurance used for personal and family needs. But the protection set up by business firms does involve many more complex details to meet legal, financial, tax and technical problems. It is life insurance custom-tailored to the individual business and probably no two plans are precisely alike in all details.

PURPOSES OF SUCH COVERAGE

There are numerous specific purposes for which business life insurance is written. Chief among these are:

(1) Key-man protection to reimburse for loss or provide replacement in the event of the death of a key employee.

(2) Partnership insurance, to retire a partner's interest at death.

(3) Corporation insurance, to retire a shareholder's interest at death.

(4) Proprietorship insurance, to provide for maintenance of a business upon the death of a sole proprietor.

(5) Insurance to aid a firm's credit status, covering the owner or key man during the period of a loan or the duration of a mortgage on property held.

(6) Where the estate of a business man consists almost entirely of his interest in a business, insurance on his life, payable to his family on his death, to provide them with ready cash and to aid in liquidating his interest in the business.

Pension plans for employees, group life insurance, disability income insurance, hospitalization, surgical and medical insurance and major medical insurance are other types of personal insurance which are utilized by business concerns to help stabilize their activities and increase operating efficiency.

FIRST STEPS

The small business contemplating the establishment of a business life insurance plan faces technical problems that call for advice. The usual procedure is to consult four experts who can make certain that every angle of the firm's interests is being safeguarded.

The four men are: the firm's attorney, its accountant, the trust officer of its bank, and its life insurance agent. The agent gives the technical advice concerning the arrangement of policies, while the others provide the essential information on which the plan is based. They also double check it when completed and assume responsibility for carrying out the legal and banking details.

Many life insurance agents who specialize in business life insurance are familiar with the whole range of problems. However, they prefer to have their client's lawyer, banker and accountant drawn in for consultation.

The owner-manager, devoting his energies to making the business a success, is not usually

in a position to analyze his insurance needs or prescribe the correct policies or policy arrangements to meet those neeeds. Such a prescription calls for highly specialized knowledge and technical advice.

TAX FACTORS

Tax factors, both income and estate, are involved in many business life insurance arrangements. These should be taken into consideration, so that the plan set up will not involve unnecessary additional taxes.

On the other hand, too much weight should not be given to the tax angles because they are constantly changing, and a plan set up today on the basis of a certain tax advantage may prove to be disadvantageous next year, if a new revenue bill is enacted or a new interpretation of existing law is made. This, too, is a matter that should be left in the hands of the experts.

RESERVE FOR EMERGENCIES

Most business life insurance plans utilize life insurance which has cash values. These cash values, growing over the years, provide the firm with a valuable reserve for emergencies, in the event of any sharp dislocation in business conditions. When necessary, the policy cash values can be used as the basis for loans. Where, for one reason or another, this type of policy is not possible, forms of term insurance may be used.

KEY-MAN INSURANCE

Almost every business has one or more men upon whom it depends heavily for its major success. Frequently it is the owner or manager. It might be the financial man, upon whose shoulders rests the responsibility of the firm's credit, and for arranging new financing or for temporary credit needs. It might be the sales manager--or, in the case of a retail shop, a leading salesman or buyer. It might be a chemist, engineer, or scientist, whose technical efforts are vital to the firm's success. It might be any employee whose death would cost the business something.

Key-man insurance is indicated for anyone whose death would cripple the business, or at least cause a setback until a replacement is secured. Such insurance provides insurance benefits at the death of this vital employee, so that the firm will have resources with which to employ and train a successor in the competitive market and to cushion the loss of profits in the meantime.

PARTNERSHIP INSURANCE

In the absence of legal safeguards to avoid dissolution, a partnership automatically dissolves at the death or shortly after the death of any one of its partners. This results in cessation of normal partnership activities and the surviving partners become what is known as "liquidating trustees."

They cannot do any new business but must confine themselves to winding up the affairs of the partnership. If they continue the business, they may become personally liable for any losses incurred should the assets not cover such losses.

There are several ways to avoid these difficulties, one of which is an adequately financed buy-and-sell agreement providing for the purchase at a prearranged valuation of the deceased partner's interest. An attorney will draw up the necessary papers carrying out the wishes of the partners.

If a buy-and-sell agreement is decided upon the next step is to fund the arrangement, which can be done effectively through business insurance. It enables the surviving partners to reorganize at once and continue in business. It liquidates the interest of the deceased partner without loss. It enables the beneficiaries of the deceased partner to secure full, fair value for his interest in the firm, at once and with a minimum of trouble. And it lends support to the credit standing of the firm.

CORPORATION INSURANCE

A corporation is not as directly and immediately affected by the death of a shareholder as is the partnership by the death of a partner, but unfortunate consequences are a distinct hazard. Unlike the partnership, the corporation is not terminated at the death of an owner, but with the transfer of the deceased stockholder's shares, new stockholders (new to management and possibly an unknown element) may come into the picture. The death of a principal stockholder may deal a severe blow to the firm's credit.

There are several ways to handle the problem. One way is an adequately financed stock sale and purchase agreement, drawn up by the firm's attorney. This may be funded by insurance. An adequate corporation insurance program on the lives of its principal shareholders, provides retirement of their interest at death. It gives the deceased shareholder's heirs full value for his interest at once and reduces the shock of changes in ownership.

This is of special concern to the small corporation with a few shareholders whose interests keep them close to the management of the business. Frequently, ownership and management are one and the same. The great bulk of the country's corporations are in this category. Large numbers of them are small, closely held businesses which adopted the corporate form primarily for its legal, tax, and continuity advantages.

By so doing, however, these owners have not escaped the death hazards which affect any business organization. Life insurance can provide the corporation with funds to purchase the interest of a stockholder at his death.

INDIVIDUAL PROPRIETORSHIP INSURANCE

Life insurance protection for the sole proprietor, to provide his dependents or heirs with cash representing the sound valuation of the business at his death and to assure continuity of the business, is as yet an undeveloped and widely neglected area of protection. Probably this is true because the need is regarded as in the province of personal life insurance.

Even in the sole proprietorships, there are special considerations that should be recognized when writing the business policy. They include:

(1) Adequate and specific provisions must be made to meet the conditions of a will or trust agreement concerning sale or liquidation of the business where such is desired.

(2) Selection of the beneficiary must be made according to the particular situation.

(3) The question of who is to pay the premiums should be determined in relation to the particular plan.

There is no set pattern; each case has to be determined on its own merits. One plan may call for sale of the business to specified employees, with the purchase money provided by the insurance. Another may provide that the business be run by the executor or the heirs. In still another, a trust company may be named as beneficiary and management control may be established.

The specific plan is important, however. Many a small business has foundered upon the death of the sole owner merely because he did not take the proper steps while alive to assure its continuance. Numerically, businesses of the individual proprietor type predominate, comprising approximately 70 percent of all units engaged in manufacturing, wholesale, retail, and service trades.

The sole proprietor who is interested in selling his business to his employees should consult with an attorney and a life insurance underwriter about the advantages of combining a pension or profit-sharing plan with a purchase agreement, funded by life insurance on the life of the business owner.

PERIODIC CHECKUP

Once established, the business life insurance plan should receive periodically a careful checkup by experts. It is important that the details of the plan be kept up-to-date at all times. Financial conditions change, tax laws vary in effect, valuations of the interests of the owners are never constant--to mention but a few of the changing conditions that can affect the plan.

Revaluations should be made whenever necessary in connection with buy-and-sell agreements and partnership and corporation policies. Every new revenue act suggests need for a special checkup to make certain the tax angles are still adequately covered. At least once each year, the plan should go through this careful screening by the life insurance agent.

FOR FURTHER INFORMATION

Readers who wish to explore this subject further may be interested in the references indicated below. This list is necessarily brief and selective. However, no slight is intended toward authors whose works are not mentioned.

"Sole Proprietorship Life Insurance," *Management Aids for Small Manufacturers* No. 131. Available from the Small Business Administration. October 1961. Free.

"Corporation Life Insurance," *Management Aids for Small Manufacturers* No. 132. Available from the Small Business Administration. October 1961. Free.

"Partnership Life Insurance," *Management Aids for Small Manufacturers* No. 133. Available from the Small Business Administration. October 1961. Free.

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SMALL BUSINESS ADMINISTRATION

Management Aids FOR SMALL MANUFACTURERS 131

Washington 25, D.C. October 1961

SOLE PROPRIETORSHIP LIFE INSURANCE

Prepared by the Institute of Life Insurance,
New York, New York

WHAT THE ONE-MAN BUSINESS FACES

There are more sole proprietorships than any other form of business organization in the United States. It is estimated that more than 70 percent of the Nation's four-and-a-half million retail, manufacturing, wholesale and service businesses in this country are owned and managed by one person.

In most cases, the State laws provide that, upon the death of a sole proprietor, his business becomes a part of his estate, to be administered by his executor or administrator and passed along to the heirs as quickly as possible--unless otherwise provided.

Thus, it is clear that the family and heirs of the owner of a one-man business face the possibility of loss, even liquidation at severe sacrifice, unless some specific plan is set up in advance of death, to assure future operation of the business, if it is to be continued.

If the proprietor dies, a number of things can be done:

(1) The business can be left to the son, widow or other heirs.

(2) It can be sold to the employees.

(3) It can be sold to outsiders.

(4) It can be continued by the executors or trustees.

(5) It can be liquidated.

PROBLEMS

Each of these procedures, unless set up under a carefully drawn plan, raises problems for the sole proprietor's heirs. Sale might be forced by either cash needs or demands of heirs and a forced sale could result in severe loss.

If the executor were to run the business, he would hire a manager who might not do the best job possible. Among other things, this manager would know the work was temporary.

The son or other heir might not be qualified to run the business. The heir might still be a minor, might have friction with other heirs or with employees, or might be handicapped by lack of working capital or credit.

If the business is transferred to employees, or outsiders, there might be controversy over valuation. Or there may be trouble over availability of funds to carry out the transfer.

Delays caused by administration, even where there is a will, could cause serious losses. Any change could disturb customer goodwill and employee morale. It could create credit difficulties.

The sole proprietor who is interested in selling his business to his employees should consult with an attorney and a life insurance underwriter about the possibility of combining a pension or profit-sharing plan with a purchase agreement. Such a plan can be funded by life insurance on the life of the business owner.

NEED FOR FUNDS

Whatever disposition is to be made of the business, there will be need for funds. Debts, taxes and administrative costs have to be met. Income for the family has to be provided.

If the family is continuing the business, someone will probably have to be hired to manage the business. And working capital will be needed, at least for a period of readjustment.

If employees are to take over, funds for their purchase of the business have to be made available, at least in part.

If the business is sold outright, working capital will be needed for the transition period. Perhaps some funds may also be needed to meet the probable discounting of assets which accompany such a sale.

IMPORTANCE OF THE TIME ELEMENT

Most of these funds are needed quickly--more quickly than they could be provided by the sale of the business unless through a forced sale, in which case there would almost certainly be a loss. The tax needs are urgent and cannot be avoided or postponed. Credit needs are likely to be even more urgent, if the business is to be maintained during the transition period.

Depending on the type of business involved, there is likely to be an immediate need for working capital. A grocery, for example, dealing in perishable goods, might require capital for immediate use.

A warehouse or iron foundry, or plant of highly specialized type, might find it so difficult to find a buyer that substantial funds would be needed to tide the business over the period of seeking a successor. A small newspaper, worth $35,000 as a going concern and with equipment alone worth that amount, without regard to goodwill, might understandably have to be sold for much less unless there were ample time to search for a successor, editor and publisher.

Many small businesses, built around some unique contribution or specialty of the proprietor, could conceivably find no buyer whatsoever. Its income-producing value would vanish overnight.

THE SOLUTION: ADVANCE PLANNING

To meet these problems the proprietor needs to set up a well planned working program for taking care of the business and the heirs at death. His plan should include:

(1) A will covering disposition of his business.

(2) A purchase and sale agreement or carefully drawn plan for disposal or continuation of the business.

(3) An estimate of the funds required to carry out the details of the plan,

Inasmuch as a will, a trust agreement, possibly a purchase and sale agreement and a life insurance program are to be written, it is evident that consultation between the insurance agent, the accountants, the trust officer and the attorney of the proprietor is advisable. These experts can determine what is needed and draw up a plan to meet the legal technicalities and financial needs involved.

The details of the plan will not necessarily follow any set pattern. For example, business life insurance for a sole proprietorship, even more than for any other type of business must be tailored to the particular case.

What the plan will involve, what kind of insurance is suitable, how it will be set up, depends on several factors. Some of them are:

(1) Type of business.

(2) Time urgency.

(3) Disposition of the business.

(4) Funds available.

(5) Probable needs in the period following death of the owner.

Where it is determined that the funds available, including existing personal life insurance, are insufficient to meet the needs as determined, business life insurance for sole proprietorships is now widely in use. A suitable business insurance program can produce the following results:

(1) Assure immediate funds to meet taxes, debts and administrative expenses.

(2) Provide income for the heirs.

(3) Equitably distribute the property value to the heirs.

(4) Enable the trustee to dispose of the business to best advantage, if the family is not taking it over.

(5) Put the family on sound financial footing, if it is assuming direction of the business.

(6) Stabilize the credit of the business.

(7) Maintain good employee relations by eliminating uncertainties and hazards.

OTHER INSURANCE NEEDS

The sole proprietorship, like all other businesses, may have need for other types of business life insurance. In some cases, the proprietor may have a key employee upon whom a share of the success of the business depends.

For example, a grocer may have a meat department under a butcher whose personal trade is quite an asset for the business as a whole. Death of such a key man could be a heavy blow to the whole business.

The owner of a small paper may be similarly situated with respect to an editor. A small manufacturer may have an inventor, chemist, engineer or other expert whose death would prove costly. Key-man life insurance gives the proprietor cash as a cushion against this type of loss.

The sole proprietor may also have the same needs as his partnership or corporate competitors in the area of supplementary insurance protection. That is his needs may be the same for group life insurance, group annuities or pensions, group hospitalization, surgical and medical insurance, group major medical, and group disability income insurance.

If his employees are sufficiently numerous, he can provide these coverages through group insurance. If his employees are few, he can set up equivalent but more expensive plans through group-written individual policies.

Interest in these supplementary plans among owners of very small business units has increased materially in recent years and

probably will continue to do so in the years ahead. Competition for good workers will be a factor, as more and more of the larger concerns provide these types of protection for their workers.

PERIODIC CHECKUP

Sole proprietorship life insurance is so definitely and closely linked with the whole program of personal insurance and personal finances of the proprietor that it should be frequently checked. Such a check helps the owner-manager to make certain it is in keeping with the requirements of the personal-business relationships at all times.

This check should be made at least once a year. It is even more important than the annual inventory of stock, in that it involves future equities and income from the business far into the future.

It is not enough to set up such a plan and then file away the papers unseen for a period of years. The plan, left unchecked, might prove not only inadequate, but actually a handicap to proper handling of affairs at the proprietor's death.

FOR FURTHER INFORMATION

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SMALL BUSINESS ADMINISTRATION

Management Aids FOR SMALL MANUFACTURERS 133

Washington 25, D.C. October 1961

PARTNERSHIP LIFE INSURANCE

Prepared by the Institute of Life Insurance
New York, New York

THE NEED FOR PARTNERSHIP LIFE INSURANCE

Since a partnership is dissolved by the death of a partner, either at once, or at best within a few months, such a death involves a serious hazard to the continuity of the business. It also involves a hazard to the interests of both the surviving partner or partners and the heirs of the deceased partner.

Upon the death of a partner, normal partnership operations cease, and the surviving partners become what is known as "liquidating trustees." This means that they cannot do any new business, but must confine themselves to winding up the affairs of the partnership.

If they continue the business they may become personally liable for all losses, or in some States, for losses in excess of the value of the partnership assets.

The heirs cannot legally enter the business and take over. However, they can demand an accounting and call for a cash settlement of their share of the firm's net worth, as represented by the deceased partner's interest.

Controversy over the valuation of this interest could well tie up a business in prolonged legal difficulties. This can be avoided through an adequately insured "buy-and-sell" agreement, establishing the valuation in advance. Through such an insurance plan, kept up-to-date at all times, the business of a partnership can be continued despite the death of a partner. Also the deceased partner's family can be assured full and immediate payment of his share of the net worth of the business.

PURPOSES

The primary purpose of business life insurance for a partnership is liquidation of the interest of any of the partners at death. It does this by establishing a clean-cut, precise plan of action, to go into effect immediately upon the death of the partner, adequately financed, according to a prearranged schedule.

There are numerous incidental purposes, such as assuring full equity for each partner's heirs, maintaining the firm's credit standing, and providing funds with which to cushion the shock which necessarily follows upon the death of any one of the firm's heads.

BENEFITS

The benefits of a partnership life insurance plan are many. If liquidation of the business is preplanned, which is not often the case, this process can be effected smoothly and without argument or difficulty.

If the aim is to continue the business, as is usually the case, this is facilitated. Indeed, practically the only way that continuity of the business can be guaranteed is through such a plan.

Each partner can be assured that his heirs will receive his full share of the business, at a valuation that he himself has approved. Controversy over valuation is thus avoided--and this removes one of the primary sources of contention in partnership settlements.

Creditors and banking circles can be assured that there will be no lapse in the credit standing of the firm, caused by the death of a partner. Without this protection, the credit of a partnership might be seriously damaged following such a death.

HOW DONE

There are various ways of establishing a partnership insurance plan, each with advantages for particular requirements.

One plan involves the purchase by each partner of a policy on the life of the other partners, each paying the premiums himself. Another plan where there are three or more partners, is to have a firm buy a policy on the life of each partner.

The question of how much premiums each should pay, the amount of insurance needed, the beneficiary arrangements, tax effects, policy assignments necessary, comprise a few of the many questions involved.

The important thing is to have all business, legal, financial and insurance needs and facilities carefully checked by experts and the final plan set up as the most effective and most economical they can devise. This is of special importance in the case of a partnership, as there is little time to move after the death of a partner.

NEEDED EXPERTS

To work out an effective plan, it is essential that the partnership utilize the services of experts--four of them. The life insurance agent, qualified on the technicalities of business insurance, the firm's lawyer, its banker, and its accountant should be drawn into the preparation of this plan.

The many details involved call for expert insurance advice. Income and estate tax effects require careful legal advice. Valuation questions and credit details call for sound financial advice.

VALUATION

Valuation of the partnership is one of the most vital of all problems to be met in setting up a partnership insurance plan. It is perhaps the most complex and troublesome of all the details involved, and commonly the one on which there is most difficulty in reaching an agreement.

This is because an attempt is being made to set up a formula under which full value is to be paid the deceased partner's heirs at some future time. The formula must be equitable and satisfy all partners or it could become the basis of long-running controversy. And yet, difficult as it may be for the partners to agree on the valuation basis today, it is clear to see that the difficulty would be even greater if its determination were put off until the tomorrow when one partner is dead and his heirs are possibly battling for a settlement based on an inflated valuation of his share in the firm.

There are many bases of valuation. Simplest is the plan which sets an arbitrary value on each partner's interest in advance. Such a plan avoids later argument, but it makes no provision for the possibly rapid shift in value through growth of the business.

If this type of plan is used, the formula for settlement could very simply be a fixed valuation for good will, plus the net book value resulting from the readily determined current value of assets, less liabilities. Good will being the element most difficult to measure, that is where controversy is most apt to develop.

Very often the plan provides that the partners will agree, at various intervals, on a revised valuation.

Another possibility is to leave the valuation to a trustee or to later arbitration under a specific arbitration plan.

Among the many possible arrangements, the one best suited to a particular firm will be determined by its specific needs.

OTHER INSURANCE NEEDS

Partnerships may also have other life insurance requirements, in addition to providing for the liquidation of a partner's interest at death.

As with any business, the partnership may have one or more key men whose death would mean a financial loss to the firm.

In the retail food business, for example, a large and thriving grocery and general market may be drawing a large part of its business from the good will created by the head butcher in the meat department. Key man life insurance on the butcher would provide the firm with funds to cushion any loss in business that might follow his death, and to hire a competent successor.

A similar need for protection also exists where a chemist, engineer, designer or technical man of any type is a key personality in the success of the business. In a brewery, the brewmaster is usually a key man. In a dress shop, either the buyer or designer might be the key personality. In a metal stamping firm, either the sales manager or the product designer. In a publication, the editor-in-chief or the advertising manager, or both, and so on, down the list of businesses.

Pension plans are becoming increasingly important today as a matter of labor relations and public relations. Where the number of employees is sufficiently large, a group annuity or

pension plan may be desirable. Where only a few are involved, some form of individual retirement policy unit could be used, with the cost shared by employer and employees in any proportion desired.

Nearly half the work force of the country is protected today under one or another form of hospitalization insurance. This protection is a matter of growing concern and expectation among workers.

A group plan for hospitalization, surgical and medical benefits, or better a major medical plan with disability income coverage added, therefore becomes a consideration for a partnership.

Credit insurance protection of various types may also be useful in the business. Credit insurance might also be indicated to cover notes and loans, which may readily be met if the business continues to operate without interruption but which might become burdensome in the event of a partner's death.

This is especially true of a business which has heavy seasonal buying commitments, involving the extensive use of credit.

Other additional coverages of special value to the partnership include business accident and sickness insurance to cover the lost services of a partner or a key man. This can be set up to prevent possible dissipation of a business while the partners are all still alive. If the partnership is heavily burdened with a mortgage on its real property, and dependent on continuity of present management to meet its commitments, life insurance protection to cover the mortgage might be valuable in the event of the death of a partner.

PERIODIC CHECK-UP

Once the partnership insurance program is set up, it is essential that it be checked periodically. Many of the elements involved in the establishment of a business insurance plan are in a constant state of flux.

Tax laws and regulations, both income and estate, change frequently and each change may have some effect on the individual business insurance plan, either as to premium payments or benefit payments, or both. Ownership changes, management changes, growth of the business, possible business declines, good will growth, valuation fluctuations--all these have a bearing in a business insurance plan, once established, and may affect or be affected by the plan.

A periodic check-up at least once a year, is just as important as regular inventory of stock or review of business operations.

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Washington D.C., August 1962

SMALL BUSINESS ADMINISTRATION
U. S. Government Agency

Management
Research Summary

INSURANCE MANAGEMENT IN SMALL RETAIL FIRMS

Prepared for the Oregon Department of Planning and Development
By *Donald A. Watson*, Assistant Director, Bureau of Business Research,
and *A. Gerlof Homan*, Research Associate, University of Oregon, Eugene, Oregon

HIGHLIGHTS

- Fire insurance premiums accounted for about 40 percent of total insurance premiums paid by the typical small retailer in the survey group. Many in the group were insured against relatively small fire losses but not against potential large losses.
- The retailers generally thought insurance agents were more interested in making a sale than in performing a service. Lack of communication was a handicap to both agents and retailers.
- Many retailers bought insurance on the same property from different agents as a matter of business reciprocity. The agents and retailers surveyed knew this was not good business practice, but they were reluctant to change.
- The adequacy of a retailer's liability insurance is extremely difficult to judge. Limits of potential loss cannot be predicted because the extent of loss is often set by jury trial.

Insurance premiums are an important item in the budget of the small retailer. Payments reported by 385 small retail firms in Oregon ranged from a low of slightly more than $100 a year to a high of more than $2,600. The average was slightly more than $260. This is probably close to 3 percent of total operating expense.

Yet the findings of the study reported in this Summary indicate that many small retailers do not have good coverage. Both retailers and insurance agents, the report concludes, should work toward better insurance programs for the small merchants.

Most of the firms surveyed had at least three general coverages--fire, automobile liability, and liability arising out of premises and operations. Only about two-thirds of the retailers were insured against crime losses, and very few carried property-in-transit (inland marine) insurance of any kind.

FIRE INSURANCE

Ninety-seven percent of the firms surveyed had at least partial coverage for fire loss. Typically, about 40 percent of a firm's total premium payment went for fire and extended (windstorm, hail, explosion, smoke, and so on) coverage. It was found that the retailers in the study were, in general, reasonably well insured against relatively small fire losses; but many had left potential large losses uninsured.

Only 157 of the 385 retailers cooperating in the study owned the buildings in which they operated. All but five of these carried fire insurance on their buildings. About 22 percent, however, were seriously underinsured.

Eighty-one of the 152 insured property owners, or 53 percent, had coinsurance clauses (if the insured carries less than a

AVAILABILITY OF THE FULL REPORT

Copies of the full report, titled "Insurance Management Problems of Small Retailers," may be purchased for $2.00 from the Bureau of Business Research, University of Oregon, Eugene, Oregon. Make checks payable to the Bureau of Business Research.

This report was prepared under the 1959 Small Business Management Research Grant Program of SBA. It may be reviewed at any SBA field office or at certain depository libraries whose addresses may be obtained from the SBA field offices or from the Small Business Administration, WASHINGTON, D. C. 20416

specified amount of insurance, he bears part of any loss himself) in their policies. Some of the firms would not have saved anything by the use of a coinsurance clause. Others, however, were either unfamiliar with its use or not convinced of its advantages.

Ninety percent of the cooperating merchants carried fire insurance on stock, though only 57 percent were fully covered. Sixty-six percent of the insured firms had coinsurance clauses in their policies.

Fire insurance on stock was often combined with other coverages. In 72 percent of the firms, the policies included extended coverage. Both extended coverage and vandalism were included in another 13 percent.

Fire insurance on equipment was carried by 82 percent of the retailers. In 16 percent of the cases, the amount was not enough to replace depreciated value. Fifty-nine percent of the firms included extended coverage. Another 22 percent included extended coverage and also vandalism and malicious mischief.

Business-interruption insurance was carried by 34 firms. The reason most often given for not having this type of coverage was lack of funds. Replacement-cost endorsement is relatively new and was found in the fire policies of only 22 firms.

• Insurance and Business Reciprocity

The effect of business reciprocity was seen in the number of policies carried on stock and equipment. In all, 547 policies were carried by 348 retailers whose stock was insured against fire. The 316 firms that carried fire insurance on equipment had a total of 407 policies.

Seemingly, when a retailer is anxious to retain the trade of an insurance agent, he is most likely to buy another fire policy on stock or equipment or both. The extra policies were often small. The premium outlay can be smaller here than for liability insurance or fire insurance on the building.

The danger of carrying several policies on the same property is that difficulties may arise from conflicting terms, or nonconcurrencies. It is important that all policies read alike in all important respects. Twenty-three cases of nonconcurrency were found in stock fire-insurance policies and 13 in equipment policies.

Both agents and retailers were aware that these multiple policies are not good business practice. But both were reluctant to change for fear of losing business.

AUTOMOBILE INSURANCE

For the retailers surveyed, automobile insurance was second to fire in premiums paid for business insurance. But many had insured their cars as a nonbusiness risk. Only two retailers who did not own cars were entirely without automobile insurance.

Three common types of automobile insurance were considered important to the study: collision, property damage, and bodily injury.

Ninety-one percent of the firms taking part in the study carried insurance to pay for direct and accidental loss to the owner's automobile in case of upset or collision with another object. Of these 351 firms, 99 had a $50- and 226 a $100-deductible provision.

About 93 percent of the retailers had property-damage insurance. Thirty-five percent had property-damage limits of $10,000; 24 percent had limits of $5,000.

All the car-owning firms carried bodily-injury automobile insurance. For this coverage, the most frequent limits were $50,000 per person and $100,000 per accident (40 percent of the firms), and $25,000 per person and $50,000 per accident (30 percent of the firms.

LIABILITY INSURANCE

Liability insurance is becoming increasingly important. Awards for damages to persons and property show a rising trend in number and amount.

Eighty-four percent of the firms surveyed had some form of business-liability insurance other than auto liability. Most policies covered several risk situations, usually property damage and bodily injury on the premises. Products liability was carried by many restaurants, service stations, and garages.

It is extremely difficult to judge the adequacy of this type of coverage for retail firms because the upper limit of the potential

loss is unpredictable. In loss by fire, for example, a building has a determinable value which the loss cannot exceed. But a liability loss is often set by a jury trial, and the trend has been for increasingly large settlements.

More than half the firms surveyed (55 percent) had property-damage limits of $10,000 or less in this type of coverage. Eighty-four firms (22 percent) had no property-damage liability insurance at all.

Eighty percent were insured against bodily injury on premises. Here, the limits ranged from $10,000 per person and per accident to $100,000 per person and $300,000 per accident. The limits used most often were $50,000 and $100,000.

Medical payment limits ranged as high as $5,000, but the most frequently used limit was $250 per person. Thirty-five percent of the firms had policies with this limit. Twenty-one percent had no coverage.

CRIME INSURANCE

The retailers surveyed did not consider high coverage as important for crime as for fire and liability. Still, 268 firms (70 percent) had a total of 393 crime-insurance policies.

The more prosperous firms--with higher volumes of sales and checkwriting and more employees handling financial matters--were more likely to have forgery and employee-dishonesty insurance than the smaller firms. The amount of burglary insurance was influenced by the value and size of the merchandise sold. For instance, furniture stores, with large, bulky items, are not subject to the same risk of burglary loss as camera and jewelry stores.

Other factors in the amount and type of crime insurance were the ratio between cash and credit sales, and the amount of cash kept on the premises. Service stations, with a large proportion of credit-card sales, do not need the same robbery-insurance limits as cash-and-carry grocery stores. Isolated stores, those making infrequent bank deposits, and those open 24 hours a day have added crime risks.

INLAND MARINE INSURANCE

Technically speaking, inland marine insurance covers property being transported or subject to being transported or moved about. Many small retail firms rarely have property in transit. The small retailer usually takes title to goods only when they have been deposited in his place of business. When the merchandise is sold, the customer usually takes title at once.

In certain types of business, however, including some retail stores, inland marine policies are widely used. They provide important coverage for the businessman who often has goods in transit or who needs all-risk coverage on certain kinds of merchandise normally kept in his place of business.

These policies are appropriate for the retailer dealing in any of the following kinds of merchandise: jewelry, cameras, furs, musical instruments, household appliances, office machinery, heating and air-conditioning equipment, sporting goods, or farm implements.

Only 55 (14 percent) of the stores had inland marine insurance. In all, there were 87 policies, including block, parcel-post, installment-sales, and sign policies.

Block policies provide insurance on loss of property on the premises, in transit, in a safe or vault at a bank or safe-deposit company, or at any other location. They also insure customers' property left with the retailer. Thirty-six of the merchants interviewed had block policies.

Thirty-two firms that shipped large numbers of packages carried parcel-post insurance with commercial insurance companies. These policies insure the safe arrival of merchandise sent either by mail or by express.

Installment sales floaters insure the merchant's interest in merchandise sold on the installment plan. Ten firms in the survey group had this type of insurance.

Only nine of the retailers had electric-sign insurance. Many did not have electric signs. Others planned to absorb any loss on their signs as a business expense. In some cases, signs were insured by the owners of the buildings (where the retailers were renters) or by commercial sign companies from whom signs were leased.

GLASS INSURANCE

About 27 percent (105) of the cooperating retailers had glass insurance. It was estimated that 12 firms which did not have glass insurance should have had some coverage. On the other hand, 35 firms which had glass insurance did not appear to need it.

THE RETAILER AND THE AGENT

A separate survey was made among a smaller number of retailers (115) in 4 cities.

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The purpose of this survey was to study the attitudes of the retailers toward insurance and insurance agents.

The picture that emerged was one of suspicion and distrust on the part of the retailers toward nearly all aspects of insurance. Many did not know what provisions their own policies included. They realized that they themselves could not easily determine what insurance they needed.

Yet they were not willing to take insurance agents into their confidence and release information needed in formulating a sound insurance program. They felt that insurance agents were more concerned with making sales than with performing a service. This distrust resulted in a lack of communication that handicapped both retailer and agent.

RECOMMENDATIONS

- Retailers could improve their insurance programs by keeping at a minimum the number of agents writing their policies. This would prevent gaps and overlapping coverages and improve service on claims.

- Policies should be reviewed regularly to make certain that the limits are high enough to take care of rising prices of merchandise and buildings, and rising amounts awarded in liability suits.

- Communication between retailers and insurance agents should be improved. Confining all policies to one agent would help, but more than that is needed.

- Many insurance agents could take a more professional approach in programming insurance. Some agents, in fact, need to know more about their own field. Agents' associations could probably help in this area. The retailer needs better accounting methods and a willingness to provide the insurance agents with needed information about the firm.

- The possibility of wider use of deductibles in fire and liability insurance should be studied.

- Special rates should be considered for retailers who keep hazards at a minimum.

- Agencies that collect and report data on insurance should consider providing more complete information on all types of losses in all kinds of businesses.

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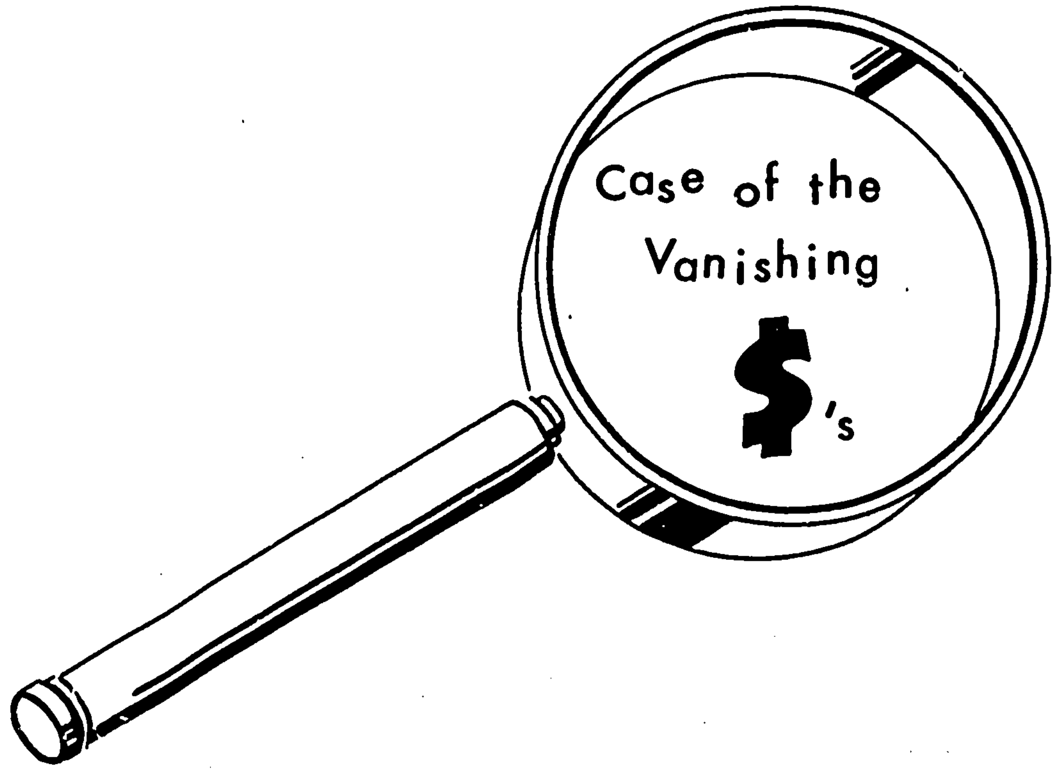
ABOUT THE STUDY

The information on which the report is based was obtained from interviews with retailers and insurance agents and from a study of government and private statistical sources. The 385 retailers cooperating in the study included proprietors of many kinds of stores in cities of various sizes. Most of them were located in the Willamette Valley of Oregon.



CASES IN POINT

Case Studies for Depth Penetration

Section

The case method has proven stimulative and effective in many administrative management courses. The following case material is suggested as a means of encouraging discussion.

It is suggested that one full session be devoted to the presentation of the topic as outlined in this manual. A case can sometimes be used to stimulate or augment the discussion period that follows the presentation. This could be one way of expanding the basic materials into an advanced course on the subject.

THE CASE METHOD OF STUDY

What is the case method? The case method is a teaching device that helps the student learn through exercising the reasoning and decision-making processes. This can be contrasted with other popular teaching techniques which place stress on learning (or memorizing) an accumulation of past knowledge on a given subject. The case method stresses thinking rather than memorizing; it is a dynamic or active method rather than a passive one.

What is a case? A case is a description of an actual or true-to-life business situation. It is a statement of facts, opinions, and judgments—in short, it is a problem.

The case method is particularly useful in teaching businessmen because it utilizes real, practical problems rather than abstract concepts. Properly used, it provides a realistic environment that causes the participant to become involved and holds his interest. It provides experience in performing essential parts of the administrative tasks without incurring the penalties of a wrong decision on the job. It develops within the individual the process of making decisions, and forces him to think analytically and constructively.

The student also learns the value of group discussion and analysis. Each member of the case discussion group contributes from his unique experience, and each gains from the others. The group knowledge and experience will exceed that of any individual participant—including the instructor.

The following checklist is suggested as an outline procedure for conducting case study and analysis:

Suggestions for Case Study

1. Read the case carefully for general content.

2. Arrange the facts of the case in order of importance.

3. Recognize and define the major problem(s) that need solution.

4. Analyze the problems and their relative importance.

5. Search for and establish alternative solutions.

6. Select the most desirable of the appropriate solutions.

7. Analyze your probable solutions—set up the pros and cons of solutions, giving value to each.

8. State your choice, decision, or final conclusion—be prepared to defend it.

9. Stipulate the plan or plans for implementing the decision.

SUPERIOR FURNITURE COMPANY[1]

The Superior Furniture Co., located in the small community of Dismuth, was started as a general merchandise store in 1918. It continued in existence through the agricultural difficulties of the twenties, but went into bankruptcy in the depression of the thirties. It was reorganized in 1935 with a large part of the investment in furniture. For the previous two years the owner worked in an independent furniture store in the town.

During World War II the farmers in the agricultural trading area prospered and a nearby military facility brought service families to the community. The store did well during the war years. In 1946 the owner's daughter married one of the former servicemen who had been stationed in the area. Upon discharge he joined the store.

Business continued to be good for the store because the area was developing as light industry moved into it. In 1935 there were five stores in town carrying furniture, but by 1946 there were nine furniture stores. In 1946 the owner and the son-in-law decided to operate a complete furniture store. The store was remodeled in 1947 and all merchandise lines other than furniture were sold. By 1950 there were fourteen stores handling furniture.

The owner's two sons, after military service and college, entered the business in 1950 and 1952 respectively. The owner of the business continued to manage the business until the end of 1955 when he retired due to illness. Up to this time the business had grown until there were three employees in the office, four salespeople, two warehouse employees, and four employees on the delivery and service trucks.

Sales had increased from $127,000 in 1947 to $361,000 in 1955. In 1950 an accounting firm had been employed to make annual statements, set up a system for handling accounts receivable, and to aid in keeping records of purchases, sales, markdowns, and gross margin. In 1953, the store was divided into departments for purposes of recordkeeping and buying consisting of bedding, sofas, chairs, tables, desks, bedroom, dining room, mirrors and lamps, floor coverings, and appliances.

In 1956 and 1957 the son-in-law handled the office activities, most of the buying, working with the accounting firm, and supervising the personnel. The

[1] From *Ten Alabama Small Retail Cases* by Harry A. Lipson, School of Commerce and Business Administration, University of Alabama under the Small Business Administration Management Research Grant Program.

two sons assisted with everything and had no particular responsibilities although one of the sons liked to work with the sales promotion plans for the store. Occasionally the sons made purchases under the guidance of the son-in-law.

By the latter part of 1957 the son-in-law suggested that an organization chart be made. This suggestion was put into practice. It was brought on by the sale of an established furniture business located in the same block but across the street from the Superior Furniture Co. This store was to be operated by a regional chain of furniture stores which had been highly successful in operating similar stores. In addition, a store on the same side of the street had been operated as a variety store and gone out of business. The building was remodeled and a former manager of a large furniture chain operating in the South opened a furniture store.

The son-in-law worried that the new competition would hurt the sales of the store. He was concerned because the profit for the store had been declining. With four families trying to live on the profits of the store, he wanted to have a basis for compensation. He thought that if each of the sons handled some of the departments they could be compensated for managing the department in terms of the net profit earned by the departments under their direction. He recognized that the warehouse and delivery departments did not show any profit, but these conditions would be offset by the effort he spent working with the office staff and generally supervising the personnel.

It was the belief of the son-in-law that the father should receive 3 percent interest on his investment plus 10 percent of the profits. The son-in-law and sons should get a proportionate share of the remainder of the profit depending upon the earnings of the departments they managed. The father of the sons was agreeable to this proposal, but wondered if his sons could manage their departments because of their lack of training and experience in making management decisions. He was willing to pay both the son-in-law and the sons a reasonable salary in addition to the percentage of the profits.

The sons thought that the son-in-law's proposal was a good one so they worked out an organization chart for the store. This chart is shown in figure 1. The son-in-law is shown as Mr. A and the sons as Mr. B and Mr. C.

Throughout 1958 an effort was made to follow this organization pattern, A, B, and C found that they were in considerable disagreement concerning the quantity and quality of the merchandise to be purchased by their respective departments. They disagreed over markups, sales events, and similar matters.

At a family conference with the accountant in early 1959 the accountant pointed out that other stores he served were expanding sales more rapidly by the

Superior Furniture Company
Planned Organization Chart

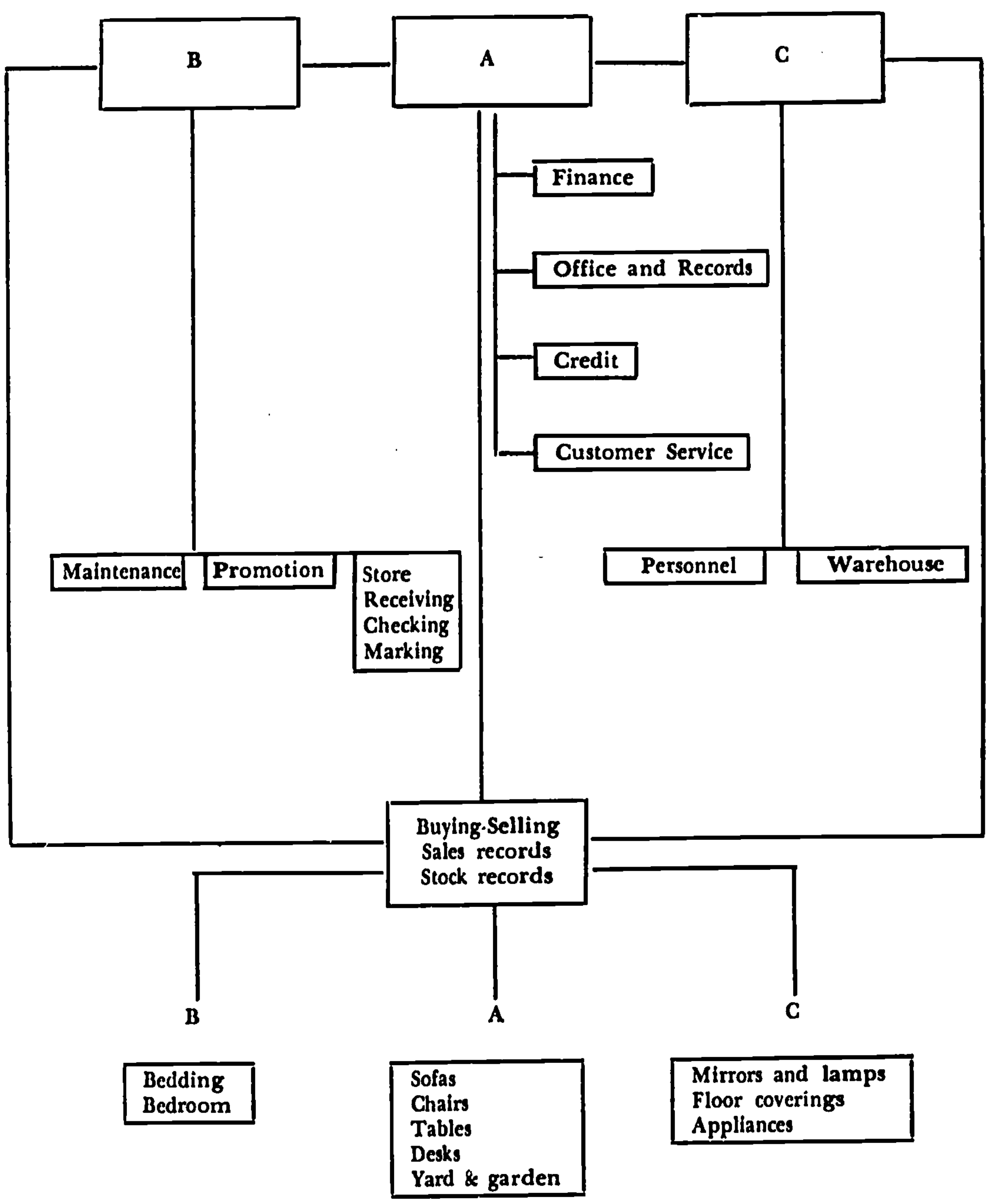


Figure 1

use of credit, other stores had a more attractive appearance, other stores were doing a better job of sales promotion, and other stores were making greater profits on their investment. He indicated Superior Furniture Co.'s declining percentage of profit for the past 3 years. His analysis was that four families were trying to live on the profits of the store. As a result, salaries had been increased in 1957 and again in 1958, more money was tied up in inventory, merchandise turnover in some departments was decreasing, more interest was being paid on loans for the higher inventory and larger accounts receivable, payments on accounts receivable were slipping, and the gross profit was lower due to larger markdowns. He recommended a tighter control on purchases, an improvement in store appearance, and improved management methods.

A, B, and C were particularly bothered by the net profit each earned in the various departments. The son-in-law believed he was earning his large net profit by astute merchandising. One of the sons believed the son-in-law actually had a bigger portion of the net profit because he was not offering merchandise of comparable quality to that which was offered in the rest of the store. He thought that the son-in-law was taking a higher markup than the merchandise warranted and using the reputation of the firm to sell the goods. The son-in-law did carry less brand name merchandise in his departments than the sons carried in their departments. The other son believed that the expenses of the store were not fairly distributed to each of the departments for he thought that he carried a larger part of the repair expense and maintenance of the service men for appliances than he should. He believed that many of the repairs being made were on the merchandise purchased by the son-in-law. Both sons thought the decline in payments on accounts receivable was the result of the son-in-law's practices.

For the next 3 months all three of the partners argued practically all of the time about every customer transaction, each purchase, and the decisions the others made. Much of this discussion took place on the sales floor, and sometimes in front of customers. It finally resulted in the son-in-law coming in one morning with an ultimatum to the brothers to work out with him a plan of operation they all could agree upon or he would leave the business.

At this point the brothers called upon their banker, an old friend of their father. The banker said that he had seen this coming for it was quite obvious that there was not any agreement on the store policies. He suggested that he talk with the son-in-law and the brothers together. That night they all met at the banker's home where, after lengthy and heated discussion, it was agreed to meet the following Sunday afternoon. Until then there was to be no public or private discussion of business problems, and the operation of the store would continue as before.

On Sunday afternoon the banker proposed that they begin to write down some of the store policies. For the next 5 hours, using a check list for store policies, the

banker would write a policy that was agreed on by the son-in-law and the two brothers. Every policy required a unanimous agreement. Having set up the method, the banker suggested that the partners meet each night at the store and continue to thrash out as many of the policies as they could write down. Each night for the next week they met at the store. The arguments were heated but the agreed-upon decisions were written concerning community relations, merchandise, promotion, customer service, personnel, and pricing.

During the week one of the partners talked with the accountant and told him how well they were getting along in making joint decisions. The accountant suggested that they meet with him the next Thursday morning to plan sales and and purchases for the next 3 months. At this meeting the accountant helped the partners prepare for each department a merchandise plan covering planned sales, planned first-of-month stocks, planned retail reductions, planned purchases, and open-to-buy.

In the course of this conference the accountant asked about the plans being made to meet the new competition. One partner stated that he had contacted a firm specializing in store fixtures and that he had some rough plans and suggestions drawn up by the architect employed by the store fixture firm. The estimate was $12,000 for changing the store front, erecting a new sign, putting tile on the floor, repainting the interior, and installing new lighting in the store. Of this amount $4,000 was for a new floor, lights, and repainting.

The accountant indicated that the working capital of the firm could not be reduced any further for store improvements. He suggested that they talk with the banker about additional bank loans. The banker stated he would be willing to make an additional amount of money available to the store provided they operated profitably and harmoniously through 1959.

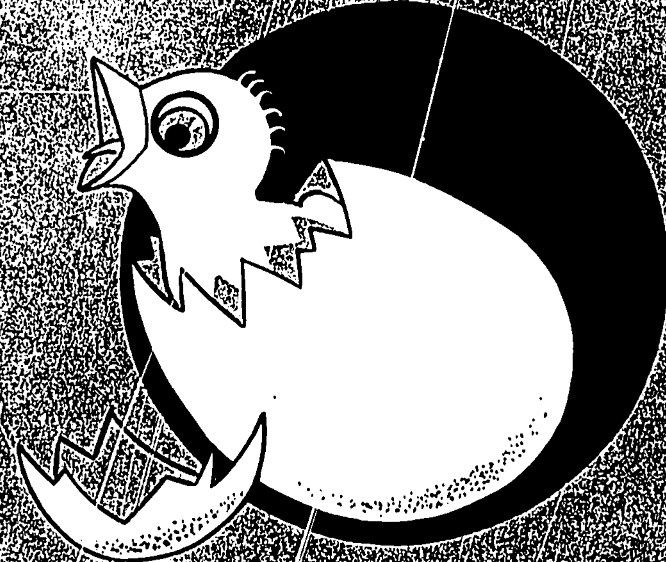
The sons and son-in-law set up a system of planned purchases and a monthly expense budget for each of the departments. Every Thursday morning the sons and son-in-law met to agree on promotions for the next week and to discuss each aspect of the business. All disagreements were hammered out in the privacy of the office and, after coming to a common agreement, they all left the meeting with an intent to carry out the planned program.

Within the meetings there was still the intense debate over the quality and brand of merchandise to be carried in the store. The son-in-law argued that the competition of the two new stores had to be met by carrying merchandise which would give the desired markup to the store. To meet this competition the son-in-law wanted to continue to "merchandise" his lines. The sons argued that manufacturers' nationally advertised merchandise with a suggested retail price was preferable because the customer knew the quality and reputation of the merchandise.

In 1959 the store showed a sizeable gain in sales, particularly in the son-in-law's departments. His earnings increased considerably but the sons' did not. The son-in-law wanted to obtain the bank loan to modernize the store appearance, but the sons did not want to continue the business under the present arrangement. Their father did not want them to leave the family business.

Suggested Questions

1. How should this family conflict be resolved?
2. Do you think that this business can support four families?
3. What policies do you think they agreed upon? Explain.
4. What recommendations would you make for scheduling planning activities in this business?
5. How should this business be organized? Did you agree with the proposal made by the sons?
6. What compensation plan should be used to pay the son-in-law, sons, and father?
7. What should be the brand policy of the store?
8. What schedule of training and plan for taking over the management responsibility should have been set up when the sons entered the business?
9. Is the role of the accountant for this store unusual or do accountants commonly give such detailed advice concerning the operations of a business?



THE INCUBATOR

A How To Do It Section

Experience has shown that people achieve maximum benefit from a conference, staff meeting or training session when a period of incubation follows the implantation of the new idea, new information, or "new slant."

This is a do-it-yourself section that will allow the participants to try out or apply the ideas and information gained from this session.

This material may be reproduced locally for distribution to course participants.

SUGGESTED INCUBATOR ASSIGNMENT

1. Review your current insurance coverage.

   How many different policies do you have?

   How many different insurance companies and agents do you have policies with?

   Do you have any overlapping coverage?

2. Plan a new insurance program to meet your current needs.

   What new coverage do you need?

   Should you discontinue coverage of some of your currently covered risks?

   What future needs should your plan include?

   How would a management succession plan affect your insurance?

   Could you consolidate any of your present policies?

   What gaps are there in your present coverage?

3. Develop a management succession plan for your business. Include a brief description of the following elements:

   A will

   Insurance coverage

   Tax considerations

   Management development

   Interim management

   Retirement plans

BIBLIOGRAPHY

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This selected bibliography is composed of books and articles that would be useful in a study of ways to safeguard your business and in planning for management succession. Most of the publications can be obtained in libraries and bookstores or from the publishers. The free SBA leaflets listed may ordinarily be obtained from the nearest SBA office. An asterisk indicates material that was of substantial value in preparing this volume.

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The addresses and telephone numbers of these field offices are listed under United States Government in the respective city telephone directories.

- GRAY — The Lesson Plan

- RUST — The Presentation

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- YELLOW — Cases in Point

- BLUE — The Incubator